UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

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In re:

Chapter 11

MPM SILICONES, LLC, et al., Case No. 14-22503-rdd

Debtors.

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B E F O R E:

HON. ROBERT D. DRAIN

U.S. BANKRUPTCY JUDGE

Corrected and Modified Bench Ruling on Confirmation of Debtors' Joint Chapter Plan of Reorganization for Momentive Performance Materials Inc. and its Affiliated Debtors.

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Good afternoon. We are back on the record in In re MPM Silicones, LLC. I had adjourned my bench ruling on confirmation of the debtors' chapter 11 plan and the related rulings in the three adversary proceedings to give the parties another day to see if they could negotiate, as between the first and the 1.5 lien holders and the debtors and the second lien holders' representatives, any settlement of their issues. I gather, since you're all here and looking fairly stony faced, that hasn't happened?

Okay. All right. So, I will give you my ruling on confirmation.

I am going to give what will sound like a series of bench rulings on five issues that remain open regarding confirmation of the chapter 11 plan and, with respect to the subordination of the senior subordinated unsecured notes, or the extent of that subordination, and the extent of the so-

called make-whole provisions in the first and 1.5 lien indentures, in the three related adversary proceedings covered by my prior order on confirmation hearing procedures. The context of each of these rulings, however, is my ruling on confirmation of the debtors' chapter 11 plan, as it has been modified on the record a couple of times during the confirmation hearing.

I have reviewed all of the evidence submitted in connection with the debtors’ request for confirmation of the plan, which includes not only the live trial record of the four-day confirmation hearing held last week, but also the declarations, exhibits, including expert reports, and deposition testimony that was admitted into evidence during that time. It's clear to me that, except for the issues that I am about to rule on and the one other issue that I ruled on last week, namely, the absolute priority rule objection to confirmation of the plan raised by the subordinated noteholders, which I decided in favor of the debtors, there are no disputes as to the confirmation of the plan. And, having reviewed the record, I am prepared to make the findings under section 1129(a) of the Bankruptcy Code required for confirmation, leaving aside, again, the five issues that I am going to address this afternoon.

I clearly have jurisdiction with regard to those issues, which arise under sections 510(a), 502(b)(2), 506(b),

1129(a) and (b) of the Bankruptcy Code, pursuant to 28 U.S.C. sections 157(a)-(b) and 1334(b), as these issues arise under the Bankruptcy Code and in the chapter 11 case, let alone that they're clearly related to the chapter 11 case.

As I noted, two of the issues also arise in three adversary proceedings, and at least one of the parties in those proceedings has stated, as required under the Local Rules, its view that the Court lacks the power to issue a final order or final determination of the issues in that proceeding. Absent the Supreme Court's ruling in Stern v. Marshall, 131 S. Ct. 2594 (2011), there would be no question that I have such power, as these are all core matters under 28 U.S.C. section 157(b)(2), each pertaining to confirmation of the debtors’ plan and/or the treatment of the claims of the first lien holders, 1.5 lien holders, second lien holders and subordinated noteholders.

I continue to have the power to issue a final order on these issues on a Constitutional basis under Stern v. Marshall. The issues all involve fundamental aspects of the adjustment of the debtor/creditor relationship. Colloquially, they pertain to how the pie of the bankruptcy estate will be divided among the groups of claimants that I just listed, not whether the estate will be augmented by a claim against a third party. Moreover, the issues clearly pertain to rights unique to bankruptcy law under section 1129(b) of the Bankruptcy Code and

sections 1129(a)(1) and 510(a) of the Code, as well as the treatment of claims under sections 502(b)(2) and 506(b) of the Code. Accordingly, under Stern v. Marshall, 131 S. Ct. 2618, I have the power to issue a final order or determination on these issues notwithstanding that this is an Article I, not an Article III, court.

These rulings, as will ultimately be memorialized in an order on confirmation as well as orders in respect of the three adversary proceedings, in each case will be a final determination by the Court.

Before I get to the rulings, I also want to note that I am providing a bench ruling here in recognition of the need for a prompt determination in this case of these issues, after having established a complete record and thought about them, I hope, thoroughly. These are ongoing businesses with thousands of employees as well as hundreds if not thousands of creditors and customers, and they deserve a prompt response. As I noted yesterday, when I give a bench ruling, at times the ruling can be lengthy with significant citation; and in those instances I normally go over the transcript and reserve the right to correct it not only as to inaccuracies by the court reporter, but also as to content, whether I said something ungrammatically, for example, or whether I wanted to say something slightly differently. If I do edit the ruling on the latter two grounds, I will separately file it as a modified

bench ruling. It won't be the transcript at that point; it will instead be a modified bench ruling, although the holdings on these issues won't change.

Let me turn to the first issue, which involves, as noted, the extent of the subordination of the senior subordinated unsecured notes. This issue comes up in Adversary Proceeding No. 14-08238 under section 510(a) of the Bankruptcy Code, which provides, "A subordination agreement is enforceable in a case under this title to the same extent that such agreement is enforceable under applicable nonbankruptcy law." It is also integral to the Court's consideration of the debtors' request for confirmation of the chapter 11 plan, because the plan has a specific interpretation of the extent of the subordination of the senior subordinated notes that the subordinated noteholders disagree with and provides, based on that interpretation, that there will be no distribution to the senior subordinated noteholders in recognition of the debtors' view, supported by the second lien holders, that their subordination agreement requires that any distribution that would otherwise go to them would have to be distributed instead to the second lien holders in full.

It thus serves as a gate-keeping issue for confirmation of the plan, because section 1129(a)(1) of the Bankruptcy Code provides that, to be confirmed, the plan must

comply with the applicable provisions of the Code, which include section 510(a).

The outcome hinges primarily if not entirely on interpretation of the relevant agreement, the senior subordinated unsecured note indenture, which, as all of the parties recognize, is governed by New York law. They also recognize that, when interpreting the indenture, the Court should apply basic New York contract law. See In re AMR Corp., 730 F.3d, 88, 98 (2d Cir. 2013), citing, among other cases, Sharon Steel Corp. v. Chase Manhattan Bank N.A., 691 F.2d 1039, 1049 (2d Cir. 1982).

Those basic contract interpretation principles are well established. Under New York law, the best evidence, and, if clear, the conclusive evidence, of the parties' intent, is the plain meaning of the contract. Thus, in construing a contract under New York law, the Court should look to its language for a written agreement that is complete, clear, and unambiguous on its face; and, if that is the case, it must be enforced according to its plain terms. J. D'Addario & Company Inc. v. Embassy Industries, Inc., 20 N.Y.3d 113, 118 (2012); Greenfield v. Philles Records Inc., 98 N.Y.2d 562, 569 (2002).

A contract is ambiguous if its terms are "susceptible to more than one reasonable interpretation." Evans v. Famous Music Corp., 1 N.Y.3d 452, 458 (2004); see also British International Insurance Co. v. Seguros La Republica, S.A., 342

F.3d 78, 82 (2d Cir. 2003), stating, "an ambiguity exists where the terms of the contract could suggest more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement and who is cognizant of customs, practices, usages and terminology as generally understood in the particular trade or business."

Thus, while in instances of ambiguity the Court may look to parole evidence, if the agreement on its face is reasonably susceptible to only one meaning, that meaning governs; a court is not free to alter the contract to reflect its personal notions of fairness and equity. Greenfield v. Philles Records Inc., 98 N.Y.2d at 569; see also In re AMR Corp., 730 F.3d at 98.

Some additional points are worth emphasizing before proceeding to the language of the indenture itself. As noted in several of the foregoing authorities, the context of the entire agreement is important. The courts have cautioned (including when construing subordination language) that one should not take an isolated provision that might be susceptible to one or more readings out of context, but should apply it instead in the context of the entire agreement, or construe it in a way that is plausible in the context of the entire agreement. See, for example, Barclays Capital, Inc. v. Giddens, 2014 U.S. App. LEXIS 15009, at *21 (2d Cir. Aug. 5, 2014); In re Tribune Company, 472 B.R. 223, 255 (Bankr. D. Del.

2012), aff'd in part, vacated in part on other grounds, 2014 U.S. Dist. LEXIS 82782 (D. Del. June 18, 2014).

It is also fundamental that every word of the agreement should, to the extent possible, be given a meaning, or, in other words, one of the most basic interpretive canons is that a contract should be construed so that effect is given to all of its provisions and no part will be inoperative or superfluous or of no significance. See, for example, LaSalle Bank N.A. v. Nomura Asset Capital Corp. 424 F.3d 195, 206 (2d Cir. 2005); Lawyers' Fund for Client Protection v. Bank Leumi Trust Co. of New York, 94 N.Y.2d 398, 404 (2000).

It is also relevant, at least to confirm what appears to be an unambiguous provision or set of provisions in a contract, to consider the parties' interpretation of the contract in practice before litigation with respect to the underlying issue. See, for example, In re Actrade Financial Technologies, Ltd., 424 B.R. 59, 74 (Bankr. S.D.N.Y. 2009), and In re Oneida, Ltd., 400 B.R. 384, 389 (Bankr. S.D.N.Y., 2009), aff'd 2010 U.S. Dist. LEXIS 6500 (S.D.N.Y. January 22, 2010).

Finally, the Court may be assisted in its understanding of the context of the contract by third party commentaries, particularly by seemingly nonpartisan industry groups like the ABA. See, for example, In re Metromedia Fiber Network, Inc., 416 F.3d 136, 139-40 (2d Cir. 2005), as well as, at least when a contract's meaning is being clarified in

context, Quadrant Structured Products Co., Ltd. v. Vertin, 2014 N.Y. LEXIS 1361, at *31-2 (N.Y. June 10, 2014).

Having laid out these basic contract interpretation principles, let me turn to the language of the senior subordinated unsecured note indenture itself, noting first that both sides in this dispute have taken the position that these terms, although their import is disputed, are, in fact, unambiguous and susceptible to a plain meaning reading.

The operative paragraph providing for the subordination of the senior subordinated unsecured notes is Section 10.01 of the indenture, which provides in relevant part, "The Company [meaning the issuer/debtor] agrees, and each Holder, by accepting a Security agrees, that the Indebtedness evidenced by the Securities, is subordinated in right of payment, to the extent and in the manner provided in this Article 10, to the prior payment in full of all existing and future Senior Indebtedness of the Company and that the subordination is for the benefit of and enforceable by the holders of such Senior Indebtedness. The Securities shall in all respects rank pari passu in right of payment with all the existing and future Pari Passu Indebtedness of the Company and shall rank senior in right of payment to all existing and future Subordinated Indebtedness of the Company; and only Indebtedness of the Company that is Senior Indebtedness of the Company shall rank senior to the Securities in accordance with

the provisions set forth herein."

"Indebtedness" is defined in the indenture at page 19 as "(1) the principal and premium (if any) of any indebtedness" -- lower case i -- "of such Person whether or not contingent, (a) in respect of borrowed money, (b) evidenced by bonds, notes debentures or similar instruments or letters of credit or banker's acceptances (or, without duplication, reimbursement agreements in respect thereof), (c) representing the deferred or unpaid purchase price of any property," and other types of debt not relevant hereto;

and then, in paragraph (2), "to the extent not otherwise included, any obligation" -- lower case o -- "of such Person to be liable for, or to pay, as obligor, guarantor or otherwise, on the Indebtedness of another Person (other than by endorsement of negotiable instruments for collection in the ordinary course of business);

“(3) to the extent not otherwise included, Indebtedness of another Person secured by a Lien" -- uppercase L -- "on any asset owned by such Person (whether or not such Indebtedness is assumed by such person); provided, however, that the amount of such Indebtedness will be the lesser of: (a) the Fair Market Value of such asset at such date of determination, and (b) the amount of such Indebtedness of such other Person;"

and then (4), another type of indebtedness that is not

relevant here; and there is a proviso that's also not relevant here, with respect to contingent obligations as deferred or prepaid revenues of purchase price holdbacks.

It is clear, therefore, from a plain reading of Section 10.01 of the indenture and the definition of "Indebtedness" that the indenture and, in particular, its subordination provision, provides for debt or claim subordination, not lien subordination.

There is a good example in the record of lien subordination, which I will get to, in the form of the Intercreditor Agreement among the second lien holders and the senior lien holders, as well as the debtors. However, it is clear from the subordination provision of Section 10.01 and the definition of "Indebtedness" that I previously quoted that the subordination of the senior subordinated unsecured notes is a subordination in respect of the payment of debt, and that the parties distinguished liens, which secure indebtedness, from indebtedness itself in several instances in the indenture, including in the definition of “Indebtedness” and “Lien,” which is found on page 21 of the indenture: "’Lien’ means with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind in respect of such asset, whether or not filed, recorded or otherwise perfected under applicable law (including any conditional sale or other title retention agreement, any lease in the nature thereof, any

option or other agreement to sell or give a security interest in and any filing of or agreement to give any financing statement under the Uniform Commercial Code (or equivalent statutes) of any jurisdiction)."

Clearly, liens differ from indebtedness in common parlance and as defined in the indenture. Liens have a life of their own; they are not a characteristic of indebtedness but, rather, secure it.

Under Section 10.01 of the indenture, the senior subordinated noteholders have subordinated their right to payment of the debt owed to them to the extent provided for in the indenture to the prior payment in full of all existing and future “Senior Indebtedness.” The issue comes down to, then, in large measure, the definition of "Senior Indebtedness" found at page 32 of the indenture, which provides, "’Senior Indebtedness’ means all Indebtedness and any Receivables Purchase Option of the Company or any Restricted Subsidiary, including interest thereon (including interest accruing on or after the filing of any petition in bankruptcy or for reorganization relating to the Company or any Restricted Subsidiary at the rate specified in the documentation with respect thereto, whether or not a claim for post-filing interest is allowed in such a proceeding) and other amounts (including fees, expenses, reimbursement obligations under letters of credit and indemnities) owing in respect thereof,

whether outstanding on the Issue Date or thereafter incurred, unless the instrument creating or evidencing the same or pursuant to which the same is outstanding expressly provides that such obligations are subordinated in right of payment to any other Indebtedness of the Company or such Restricted Subsidiary, as applicable."

That last clause is the first proviso to “Senior Indebtedness.” That is, Senior Indebtedness means all Indebtedness “unless the instrument creating or evidencing the same or pursuant to which the same is outstanding expressly provides that such obligations are subordinated in right of payment to any other Indebtedness of the Company.” In other words, this first proviso states that indebtedness under the senior subordinated unsecured notes will not be subordinated to indebtedness under instruments that expressly provide that such indebtedness is itself subordinated debt.

Next, the indenture’s definition of "Senior Indebtedness" sets forth a series of other exceptions or provisos, stating, "provided, however, that Senior Indebtedness shall not include, as applicable: (1) any obligation of the Company to any Subsidiary of the Company other than any Receivables Repurchase Obligation or any Subsidiary of the Company to the Company or any other Subsidiary of the Company [that is, intercompany debt is not Senior Indebtedness];

"(2) any liability for Federal, state, local, or other

taxes owed or owing by the Company or such Restricted Subsidiary [that is, tax obligations are not Senior Indebtedness];

"(3) any accounts payable or other liability to trade creditors arising in the ordinary course of business (including guarantees thereof or instruments evidencing such liabilities)" [that is, trade debt is not Senior Indebtedness];

"(4) any Indebtedness or obligation of the Company or any Restricted Subsidiary that by its terms is subordinate or junior in any respect to any other Indebtedness or obligation of the Company or such Restricted Subsidiary, as applicable, including any Pari Passu Indebtedness;

"(5) Any obligations with respect to any Capital Stock; or

"(6) any Indebtedness Incurred in violation of this Indenture, but as to any such Indebtedness Incurred under the Credit Agreement, no such violation shall be deemed to exist for purposeless of this clause (6) if the holders of such Indebtedness or their Representative shall have received an Officer's Certificate to the effect that the Incurrence of such Indebtedness does not (or, in the case of a Revolving Credit Facility thereunder, the Incurrence of the entire committed amount thereof at the date on which the initial borrowing thereunder is made, would not) violate this Indenture."

The subordinated noteholders contend that clause (4)

of the definition of “Senior Indebtedness” which I have just quoted provides that (notwithstanding clause 4’s failure to refer to liens) any indebtedness that would otherwise be Senior Indebtedness would not have the benefit of the indenture’s subordination provision because of the fact that it is secured by a junior lien

Again, clause (4) to this series of additional provisos to the definition of "Senior Indebtedness" excludes any “Indebtedness or obligation of the Company or any Restricted Subsidiary that by its terms is subordinate or junior in any respect to any other Indebtedness or obligation of the Company or such Restricted Subsidiary, as applicable.”

The subordinated noteholders contend (and it is basically their only argument) that the foregoing "junior in any respect" language would pick up, given the broad meaning of "in any respect," liens that are junior to other liens, and accordingly, indebtedness secured by such liens.

The debtors disagree, arguing that, when viewed pursuant to the contract interpretation principles that I have stated, clause (4) of this second group of provisos to the definition of “Senior Indebtedness” pertains only to debt subordination and not to lien subordination, consistent with the distinction throughout the indenture between liens and debt, on the one hand, and liens that secure such obligations, on the other, starting with Section 10.01.

After reviewing the indenture and the commentaries and other documents that were admitted into evidence in connection with this dispute, I agree with the debtors' interpretation of clause (4). I do so for a number of reasons, but primarily because of the wording of the clause itself and the fundamental contract interpretation principle that no material term of an agreement should be superfluous under one party's construction where it has a meaning under the other's, or, in other words, that the contract should be read to give effect to all of its provisions. See, again, LaSalle National Bank Association v. Nomura Asset Capital Corp., 424 F.3d at 206; Lawyers' Fund for Client Protection v. Bank Leumi Trust Co., 94 N.Y.3d at 404.

Under the definition of Senior Indebtedness that I've quoted, the parties first excluded Indebtedness where "the instrument creating or evidencing the same or pursuant to which the same is outstanding expressly provides that such obligations are subordinated in right of payment to any other Indebtedness of the Company." Then, in clause (4) of the definition, the parties further excluded "any Indebtedness or obligation of the Company or a Restricted Subsidiary that by its terms is subordinated or junior in any respect to any other Indebtedness or obligation of the Company." The subordinated noteholders' reading of clause (4) would swallow up the first exclusion that I have quoted. That is, under their interpretation, as long as any rights of a creditor are junior

to any other creditor’s rights, such as in respect of a junior-in-time or junior-by-agreement lien, the creditor’s indebtedness is not Senior Indebtedness entitled to the benefit of section 10.01. This broad reading of the exclusion in clause (4) would render the definition’s first exclusion of expressly contractually subordinated debt superfluous.

On the other hand, the debtors’ interpretation of clause (4), which is that it applies to obligations that are by their terms subordinate even if not expressly so stated in the instrument creating the obligation, permits both exceptions to “Senior Indebtedness” to have a separate purpose. For example, obligations made subordinate to other obligations in a separate agreement, like an intercreditor agreement, or obligations that do not expressly state that they are subordinate to other obligations but are so by their terms, such as a “last out” facility in which one tranche of debt is to be paid after the rest of the debt under the same note, would fall within clause (4)’s exception but not into the first, introductory exception under the debtors’ reading of the definition of Senior Indebtedness.

The debtors’ interpretation also tracks the plain terms of clause (4), noting the difference between a debt and a lien that secures a debt. Thus clause (4) excepts from the definition of “Senior Indebtedness “any Indebtedness or obligation of the Company or a Restricted Subsidiary that by

its terms is subordinate or junior in any respect to any other Indebtedness or obligation." (Emphasis added.) The highlighted word "its" refers to the terms of the Indebtedness or the obligation -- which are separate from the terms of a lien, mortgage, security interest, encumbrance, etc. – as being junior to any other Indebtedness or obligation, not to the terms of a lien being junior to any other lien.

The debtors also correctly point out that the commentary to the ABA model subordinated unsecured note indenture, appearing in Committee on Trust Indentures and Indenture Trustees ABA Section of Business Law, "Model Negotiated Covenants and Related Definitions," 61 Bus. Law. 1439 (Aug. 2006), states that the form of clause (4) should be omitted if the obligor is "issuing junior subordinated securities." Id. at 62. Again, that is, the emphasis is on debt subordination, not lien subordination, junior subordinated securities being debt that is subordinated in any way by its terms to other debt. The commentary does not state that the clause should alternatively be omitted if the subordinated debt is intended to be pari passu with debt secured by a lien junior to another lien granted by the issuer.

The debtors' reading is also consistent with the rest of the indenture and the context of its subordination provision. The rationale, according to the subordinated noteholders, of an additional carve-out from Senior

Indebtedness for indebtedness secured by a junior lien is the concern that junior lien financings could effectively overcome or get around or fit into a loophole in contracts pursuant to which one group of debt holders subordinate their debt to another. The second lien indebtedness would be senior debt, that is, layered ahead of the senior subordinated notes although secured by only a junior lien that, based on the value of the collateral, might be largely or entirely undersecured, something that senior subordinated unsecured noteholders would not necessarily want.

It does not appear, however, that there is any anti-layering provision in this indenture responsive to that underlying concern. To the contrary, there are covenants in the indenture that deal with the incurrence of additional debt, in section 4.03, the incurrence of additional liens, in section 4.12, and a limitation, in section 4.13, on senior or pari passu subordinated indebtedness that permit both the issuance of the second lien notes and, more importantly, permit them to be senior to the subordinated notes regardless of whether they were secured by a lien. Notwithstanding those specific provisions, however, the subordinated noteholders have proposed an interpretation of clause (4) in the definition of “Senior Indebtedness” that would essentially override those provisions and exclude the second lien notes from the benefit of Section 10.01 merely because they were secured.

Moreover, the commentary upon which the senior subordinated noteholders base their argument that clause (4) was intended to close a loophole presented by junior lien financings points to the need, if one wants to exclude debt secured by a junior lien from the benefit of a subordination provision, to do so in an anti-layering covenant.

That is the case in the Fitch commentary, at page 275, which is attached as Exhibit L to Mr. Kirpilani's declaration, as well as the presentation to an American Bankruptcy Institute panel from 2006 attached as Exhibit J to his declaration, at pages 13-14. Indeed, the Thompson Reuters Legal Solutions Practical Law excerpt attached as Exhibit H to Mr. Kirpilani's declaration states at pages 4-5 that the better solution to deal with the concern about not being subordinated to second lien debt would be to place the exclusion in the anti-layering covenant itself or to add a new anti-layering provision.

The senior subordinated noteholders point to Section 1.04 of the indenture, which is entitled "Rules of Construction" and includes as one of the parties' rules of construction, in clause (f), the following: "[U]nsecured Indebtedness shall not be deemed to be subordinate or junior to Secured Indebtedness [and thus excluded from the definition of Senior Indebtedness] merely by virtue of its nature as unsecured Indebtedness." They suggest that the absence of another, similar provision in the indenture, which <u>does</u> appear

in the 2006 ABA’s “Model Negotiated Covenants and Related Definitions” discussion, 61 Bus. Law. at 71, providing that “[S]secured Indebtedness shall not be deemed to be subordinate or junior to any other secured Indebtedness merely because it has a junior priority with respect to the same collateral,” establishes, under the principle of expressio unius est exlusio alterius, that the parties meant to exclude debt secured by a junior lien from the reach of the subordination provision.

However, I disagree with that interpretation. It seems to me that, instead, given the clear resolution of the parties’ anti-layering rights, the plain meaning of the definition of "Senior Indebtedness" and the principle evident throughout the indenture that liens secure debt and are not themselves debt, there would be no need in the “Rules of Construction” section to have such a provision specifically <u>include</u> debt secured by a junior lien as Senior Indebtedness, in contrast to the need to add Section 1.04(f), which pertains to debt, not liens. In any event, it is clear from the ABA commentary, which dates from August 2006 -- just a few months before the issuance of the senior subordinated unsecured notes -- and other presentations attached to Mr. Kirpilani’s declaration that issues pertaining to the subordination of unsecured debt to debt secured by junior liens were still evolving when the senior subordinated unsecured notes were issued; there was no well established standard form that might add a meaningful context to the

indenture’s plain terms and internal consistency. Cf. Quadrant Structured Products Co., Ltd. V. Vertin, 2014 N.Y. LEXIS 1361, at *31-2 (relying, in addition to considerable precedent, on model no-action clause produced by the Ad Hoc Committee for Revisions of the 1983 Modified Simplified Indenture that predated the indenture at issue by 10 years).

The subordinated noteholders’ interpretation of “Senior Indebtedness” also would lead, to the anomalous result that their notes would be subordinated to senior unsecured debt (in this case, as suggested above, including the second lien debt, which, when issued, was unsecured because it had only a springing lien), but would cease to be subordinated when that lien sprung or when such debt was issued on a secured basis. There is no logical reason for such a distinction, notwithstanding the subordinated noteholders' attempt to find one.

The subordinated noteholders next contend that, even under the debtors’ interpretation of “Senior Indebtedness,” the Intercreditor Agreement entered into among the debtors, the second lien holders and the first lien and 1.5 lien holders, among others, and attached as Exhibit C to Mr. Kirpilani’s declaration, goes beyond lien subordination (which I have found does not fit within the exception to “Senior Indebtedness”), providing, in essence, for the subordination of the second lien holders’ debt to the debt secured by the liens of the first and

1.5 lien holders and any other debt that might be secured by senior liens.

The Intercreditor Agreement clearly does restrict the rights of the second lien holders, two of those restrictions having been highlighted by the suborindated noteholders. First, it provides that the second lien holders’ right to the shared collateral is subordinate to the senior lien holders’ right to such collateral, even if it turns out that the liens securing the senior lien debt are not perfected or enforceable. Second, it provides in paragraph 4.04 that the second lien holders shall turn over to the senior lien holders any recoveries that they obtain not only on account of their contractual liens on the shared collateral, but also on account of judicial liens that they may obtain.

However, contrary to the interpretation offered by the subordinated noteholders that these provisions of the Intercreditor Agreement are debt subordination provisions, they pertain to lien subordination, governing rights in respect of the shared collateral. Intercreditor agreements of this nature that pertain to secured creditors' lien rights are commonly geared to those rights whether or not the liens are perfected. The parties are certainly free to, and do, agree that their contractual liens, which they have mutually verified, are effective as among each other, even if such liens later prove to be generally ineffective because of a debtor's lien

avoidance powers. The focus still is on the collateral that was agreed to be secured by the liens. See In re Ion Media Newworks, Inc., 419 B.R. 585, 594-95 (Bankr. S.D.N.Y. 2009) ("By virtue of the Intercreditor Agreement, the parties have allocated among themselves the economic value of the FCC licenses as 'Collateral' (regardless of the actual validity of liens in these licenses.)").

Similarly, it is typical of intercreditor agreements among secured parties that rights to enforce interests in the collateral are, as they are here, thoroughly addressed. Accordingly, a provision stating that collections on a judicial lien (as well as from enforcement of the second lien holders' contractual lien) shall be turned over to the senior lien holders are common in shared collateral agreements, given that control over the collateral is a fundamental aspect of such agreements. See, for example the American Bankruptcy Institute presentation attached as Exhibit I to Mr. Kirpilani's declaration, at page 25, listing intercreditor agreement provisions that promote "first lienholders' desire to 'drive the bus' in respect to remedies against the shared collateral."

In contrast, Section 5.04 of the Intercreditor Agreement provides that nothing in that agreement alters the second lien holders' rights in their capacity as <u>unsecured</u> creditors, again highlighting the distinction between lien subordination and debt subordination.

While there is no interpretive language contemporaneous with the parties’ entry into the senior subordinated unsecured note indenture, the parties' subsequent actions further support the debtors’ reading of the subordination provision's reach. For example, a substantial portion of the subordinated notes, roughly $118 million in face amount, was exchanged in 2009 at a discount of at least 60 percent for second lien notes, which is inconsistent with the subordinated noteholders’ present argument that those notes are pari passu.

In addition, the trustees for the senior subordinated notes took no action with respect to the issuance of the second lien debt or the springing of the lien securing it, although arguably under the subordinated noteholders' current interpretation the debtors’ disclosures with respect to the second lien notes -- that they were senior in right of payment to the subordinated notes -- was inaccurate. It is clear from the exhibits to the responses by the ad hoc committee of second lien holders and Apollo, as well as the debtors’ submissions, that such disclosure was clear in the company's 8-K, 10-Ks, and prospectuses.

It is also the case that, under the subordinated noteholders' broad interpretation of clause 4’s exception to “Senior Indebtedness,” the debt under the debtors’ current first and 1.5 lien notes also would not benefit from Section

10.01's subordination provision, notwithstanding that the indenture's definition of "Designated Senior Indebtedness" would include the first and 1.5 lien notes. In other words, the definition of "Designated Senior Indebtedness" is not integrated into the definition of "Senior Indebtedness" as proposed by the subordinated noteholders, again rendering their broad interpretation of clause 4's exception to such definition highly unlikely in the context of the entire indenture.

The debtors, the ad hoc committee of second lien holders, and Apollo in its capacity as a second lien holder have also argued, in their briefs at least, that the subordinated noteholders are estopped by laches or other equitable principles from making the arguments that they are making now, given their silence in the face of the issuance of over a billion dollars of second lien debt that was widely disclosed to be senior in right of payment to the senior subordinated unsecured notes. At oral argument, the debtors and the second lien holders seem to have walked back on that argument, however, and I believe that it would not apply here under the case law, in any event, in light of the need to establish conduct upon which reliance is based and the absence of a factual record to show such reliance. See, for example, River Seafoods, Inc. v. J.P. Morgan Chase Bank, 796 N.Y.S.2d 71, 74 (1st Dept. 2005) (stating elements of equitable estoppel under New York law), and Eppendorf-Netheler-Hinz GMBH v.

National Scientific Supply Company Inc., 14 Fed. Appx. 102, 105 (2d Cir. July 13, 2001) (stating elements of laches under New York law).

But, based on the plain meaning of Section 10.01 and the definition of “Senior Indebtedness,” and, secondarily, the distinction throughout the indenture, as well as when the relevant provisions are read context, between lien rights and the subordination of debt, I conclude that the second lien holders’ notes are “Senior Indebtedness” and, therefore, entitled to the benefit of the subordination provision of Section 10.01 of the indenture.

The next two issues pertain to a different set of agreements that are subject to the same rules of contract interpretation that I’ve previously summarized and won’t repeat, as both operative sets of agreements -- indentures and notes -- are governed by New York law. The two issues involve the rights of the indenture trustees, and therefore the holders, of the first and 1.5 lien holders to a so-called contractual “make-whole” claim, or, barring such a claim, a common law claim for damages, based on the debtors’ payment of their notes before the original stated maturity of the notes. The first and 1.5 lien holders’ rights to such a claim are in the first instance governed by the respective indentures and notes, which, as relevant, contain the same provisions.

If, in fact, the trustees are entitled to such a claim that is enforceable in bankruptcy, it will increase the amount of the replacement notes to be issued to the first and 1.5 lien holders as their distribution under the debtors’ chapter 11 plan. That is, the plan leaves open, now that the classes of first and 1.5 lien holders have rejected the plan, for the Court to decide whether the first and 1.5 lien holders’ allowed claim includes a make-whole amount, whereas, if those classes had accepted the plan they would have received a cash distribution in the amount of their allowed claims specifically without any make-whole amount.

The indentures for both sets of notes provide in Section 3.01, captioned “Redemption,” that "the Notes may be redeemed, in whole, or from time to time in part, subject to the conditions and at the redemption prices set forth in paragraph 5 of the form of Notes set forth in Exhibit A and Exhibit B hereto, which are hereby incorporated by reference and made a part of this Indenture, together with accrued and unpaid interest to the redemption date."

Section 3.02 of each indenture states, "Applicability of Article. Redemption of Notes at the election of the Issuer or otherwise, as permitted or required by any provision of this Indenture, shall be made in accordance with such provision and this Article."

Section 3.03 sets forth the procedure pursuant to

which the issuer, that is the debtors, "shall elect to redeem Notes pursuant to the optional redemption provisions of paragraph 5 of the applicable Note."

Section 3.06 of the indentures, entitled "Effect of Notice of Redemption," states, "Once notice of redemption is delivered in accordance with Section 3.05, Notes called for redemption become due and payable on the redemption date and at the redemption price stated in the notice, except as provided in the final sentence of paragraph 5 of the Notes."

Section 3.09 of each indenture, in contrast to the optional or elective redemption under sections 3.01 and 3.03 of the indentures and paragraph 5 of the notes, provides for a special mandatory redemption on the terms set forth in Section 3.09.

Paragraph 5 of the form of first and 1.5 lien notes states, "Optional Redemption. Except as set forth in the following two paragraphs, the Notes shall not be redeemable at the option of MPM prior to October 15, 2005. Thereafter, the Notes shall be redeemable at the option of MPM, in whole at any time or in part from time to time” as provided therein. And then it states, "In addition, prior to October 15, 2015, the Issuer may redeem the Notes at its option, in whole at any time or in part from time to time, upon not less than 30 nor more than 60 days' prior notice delivered electronically or mailed by first-class mail to each holder's registered address, at a

redemption price equal to 100% of the principal amount of the Notes redeemed plus the Applicable Premium as of, and accrued and unpaid interest and Additional Interest, if any, to, the applicable redemption date (subject to the right of the Holders of record on the relevant record date to receive interest due on the relevant interest payment date)."

"Applicable Premium" is separately defined in the indentures as follows: "With respect to any Note on any applicable redemption date, the greater of: (1) 1% of the then outstanding principal amount of such Note and (2) the excess of: (a) the present value at such redemption date of (i) the redemption price of such Note, at October 15, 2015 (such redemption price being set forth in paragraph 5 of the applicable Note) plus (ii) all required interest payments due on such Note through October 15, 2015 (excluding accrued but unpaid interest), computed using a discount rate equal to the Treasury Rate as of such redemption date plus 50 basis points; over (b) the then outstanding principal amount of such Note."

The indenture trustees for the first and 1.5 lien notes argue that the chapter 11 plan's payment of the holders with replacement notes entitles them to the Applicable Premium, as they will receive such notes before October 15, 2015. They contend that such payment would be an optional or elective redemption under the provisions of the indentures and notes that I have just read.

As I've noted and will discuss later, the trustees for the first and 1.5 lien notes also argue that, even if they are not entitled by contract to an Applicable Premium constituting a make-whole under these circumstances, they nevertheless have a claim under otherwise applicable law or the first sentence of paragraph 5 of the notes, which they contend is a "non-call" covenant, that is triggered by the debtors' early payment of their notes in the form of replacement notes under the plan, although the amount of such claim, or formula therefor, is not set forth in the indentures or the notes.

Let me address the Applicable Premium argument first. It is well established that when considering the allowance of a claim in a bankruptcy case the court first considers whether the claim would be valid under applicable nonbankruptcy law, and then, second, if the claim is valid under applicable nonbankruptcy law, whether there is any limitation on or provision for disallowance of the claim under the Bankruptcy Code. See Ogle v. Fidelity & Deposit Company of Maryland, 586 F.3d 143, 147-48 (2d Cir. 2009); HSBC Bank U.S.A. v. Calpine Corp., 2010 U.S. Dist. LEXIS 96792, at *18 (S.D.N.Y. Sept. 15, 2010).

It is well settled under New York law, which is, again, the law governing these agreements, that the parties to a loan agreement, indenture or note can amend the general rule under New York law of "perfect tender" to provide for a

specific right on behalf of the borrower or issuer to prepay the debt in return for agreed consideration that compensates the lender for the cessation of the stream of interest payments running to the original maturity date of the loan. Without that contractual option, under the New York rule of perfect tender the borrower/issuer would be precluded from paying the debt early. See U.S. Bank National Association v. South Side House LLC, 2012 Dist. LEXIS 10824, at *12-13 (E.D.N.Y. January 30, 2012), as well as Northwestern Mutual Life Insurance Company v. Uniondale Realty Associates, 816 N.Y.S.2d 831, 835, 11 Misc. 3d 988, 984 (N.Y. Sup. Ct. 2006). See generally Charles & Kleinhaus, "Prepayment Clauses in Bankruptcy," 15 Am. Bankr. Inst. L. Rev. 537, 541 (Winter 2007) ("Charles & Kleinhaus"), and the cases cited therein at 541 n.13, applying New York's perfect tender rule.

It is also well-settled law in New York that a lender forfeits the right to such consideration for early payment if the lender accelerates the balance of the loan. The rationale for this rule is logical and clear: by accelerating the debt, the lender advances the maturity of the loan and any subsequent payment by definition cannot be a prepayment. In other words, rather than being compensated under the contract for the frustration of its desire to be paid interest over the life of the loan, the lender has, by accelerating, instead chosen to be paid early. See U.S. Bank National Association v. South Side

House, 2012 U.S. Dist. LEXIS 10824, at *13-14, and the cases cited therein, including In re LHD Realty Corp., 726 F.2d 327, 331 (7th Cir. 1984); In re Solutia, Inc., 379 B.R. 473, 487-88 (Bankr. S.D.N.Y. 2007); In re Granite Broadcasting Corp., 369 B.R. 120, 144 (Bankr. S.D.N.Y. 2007); and Northwestern Mutual Life Insurance Company v. Uniondale Realty Associates, 816 N.Y.S.2d at 836.

There are two well-recognized exceptions to that proposition. The first is agreed not to apply here, namely when the debtor intentionally defaults in order to trigger acceleration and evade the prepayment premium or make-whole, the debtor will remain liable for the make-whole notwithstanding acceleration of the debt. See Sharon Steel Corp. v. The Chase Manhattan Bank. N.A., 691 F.2d 1039, 1053 (2d Cir. 1982). Here, even if the trustees had not conceded this point, it is clear that the debtors’ bankruptcy is not simply a tactical device to deprive the first and 1.5 lien holders of a make-whole claim.

The second exception, which is at issue here, is when a clear and unambiguous clause calls for the payment of a prepayment premium or make-whole even in the event of acceleration of, or the establishment of a new maturity date for, the debt. See, again, U.S. Bank National Association v. South Side House, 2012 U.S. Dist. LEXIS 10824, at *14-16 and *23; Northwestern Mutual Life Insurance Company v. Uniondale

Realty Associates, 816 N.Y.S.2d at 836, and the cases cited therein. Thus, the first and 1.5 lien holders' right to an Applicable Premium, or make-whole, hinges on whether the relevant sections of their indentures and notes provide with sufficient clarity for the payment of such premium after the maturity of the notes has been accelerated.

Critically important, therefore, is another provision of the indentures, Section 6.02, which provides generally that the trustee or the holders of at least 25 percent of principal amount of the outstanding notes, upon an event of default, can elect to accelerate the notes, but also states, "If an Event of Default specified in Section 6.01(f) or (g) with respect to MPM [which includes the debtors' bankruptcy] occurs, the principal of, premium, if any, and interest on all the Notes shall ipso facto become and be immediately due and payable without any declaration or other act on the part of the Trustee or any Holders."

The form of note attached to the indentures also provides, in paragraph 15, "If an Event of Default relating to certain events of bankruptcy, insolvency or reorganization of the Issuer occurs, the principal of, premium, if any, and interest on all the Notes shall become immediately due and payable without any declaration or other act on the part of the Trustee or any Holders."

(Section 6.02 in the indentures also provides, in its

final sentence, "The Holders of a majority in principal amount of outstanding Notes by notice to the Trustee may rescind any such acceleration with respect to the Notes and its consequences," and the last sentence of paragraph 15 of the notes states, "Under certain circumstances, the Holders of a majority in principal amount of the outstanding Notes may rescind any such acceleration with respect to the Notes and its consequences." The first and 1.5 lien trustees’ arguments to rescind acceleration of the notes are discussed in the third section of this ruling)

In light of the automatic acceleration of the notes under Section 6.02 of the Indentures, as also obliquely referenced in paragraph 15 of the notes, upon the debtors’ bankruptcy filing, the debtors and the second lien holders contend that the maturity date of the notes has been contractually advanced and, thus, under New York law the first and 1.5 lien holders, having provided for acceleration in the applicable agreements, bargained for prepayment of the notes upon the event of the debtors’ bankruptcy and therefore forfeited their right to the Applicable Premium.

(In addition, the debtors and the second lien holders contend that the debtors' payment of the first and 1.5 lien holders as required by the Bankruptcy Code before the original maturity of the notes (or at least before October 15, 2015) is not elective or voluntary, and, therefore, again, does not

subject the debtors to the Applicable Premium owed upon an elective redemption under the express terms of Sections 3.02-3.03 of the indentures and paragraph 5 of the notes. The debtors have the option under section 1124 of the Bankruptcy Code, however, to reinstate the first and 1.5 lien notes rather than pay them with substitute consideration, under a chapter 11 plan. In addition, the notice requirements of Bankruptcy Rule 2002 arguably functionally track the election/notice process provided in sections 3.03 and 3.05 of the indentures. Thus, I have not further considered this argument of the debtors and second lien holders in light of the efficacy of their first argument.)

As noted previously, it is “well-settled law,” South Side House, 2012 U.S. Dist. LEXIS 10824, at *12, that, unless the parties have clearly and specifically provided for payment of a make-whole (in this case the Applicable Premium), notwithstanding the acceleration or advancement of the original maturity date of the notes, a make-whole will not be owed. Such language is lacking in the relevant sections of the first and 1.5 lien indentures and notes; therefore, they do not create a claim for Applicable Premium following the automatic acceleration of the debt pursuant to Section 6.02 of the indentures. In addition to the cases that I have already cited for this proposition, see In re Madison 92nd Street Associates, LLC, 472 B.R. 189, 195-96 (Bankr. S.D.N.Y. 2012); In re

LaGuardia Associates LLP, 2012 Bankr. LEXIS 5612, at *11-13 (Bankr. E.D. Pa. Dec. 5, 2012); In re Premiere Entertainment Biloxi, LLC, 445 B.R. 582, 627-28 (Bankr. S.D. Miss. 2010), and the cases cited therein, all of which interpret New York law, and some of which involve automatic acceleration clauses, which, as noted by the district court in South Side House, have the same negating effect as the voluntary exercise of an acceleration right, given that such clauses were negotiated by the parties. 2012 U.S. Dist. LEXIS 10824, at *20-23. See also In re AMR Corporation, 730 F.3d at 101, in which the Second Circuit made clear that such an automatic acceleration provision operates by the choice of the indenture trustee as much as the issuer/debtor; that is, such contractual automatic acceleration is not voluntary on the issuer’s part because it is an enforceable covenant, including not being subject to invalidation under any section of the Bankruptcy Code, such as section 365(e), which would negate so-called ipso facto provisions triggered by a debtor's bankruptcy filing.

The trustees for the first and 1.5 lien holders try to get around the problem that their documents do not contain sufficient language triggering an Applicable Premium after acceleration in a couple of ways, one of which is to refer to a discussion in In re Chemtura Corporation, 439 B.R. 561, 596-02 (Bankr. S.D.N.Y. 2010), in which Judge Gerber evaluated the settlement of a make-whole dispute that was opposed by those

who contended that the beneficiaries of the settlement, who were receiving a range of 39 and 43 percent of their make-whole claim under it, should really recover nothing or at least far less than that amount on account of such claims.

The trustees contend that Judge Gerber concluded that a covenant triggering a make-whole amount upon a prepayment by a date certain would be a specific enough of a reference to the make-whole’s being owed, notwithstanding the acceleration of the debt, to satisfy the explicitness requirement in the cases that I have previously cited.

I should note, however, that, in addition to the settlement context in which Judge Gerber gave his analysis, where he considered only whether the settlement lay within the lowest bounds of reasonableness, he was focusing in Chemtura not on a specific date like the pre-October 15, 2015 date set forth in paragraph 5 of the notes here, but, rather, on a provision that was triggered off a differently defined maturity date than the original maturity date, thus keying liability for the make-whole back to the need, as stated in the cases that I have cited, to state clearly that the premium would be owed notwithstanding the acceleration of the original maturity date. Id. at 601

That is not the case under the notes and the indentures here. Indeed, in each of the reported cases that quote language that would be explicit enough to overcome the

waiver of the make-whole upon acceleration under New York law, more was required than is contained in the relevant sections of the indentures and notes that I have quoted -- either an explicit recognition that the make-whole would be payable notwithstanding the acceleration of the loan or, as stated by Charles & Kleinhaus, a provision that requires the borrower to pay a make-whole whenever debt is repaid prior to its original maturity, which is in essence what Judge Gerber was referring to in the Chemtura case. See Charles & Kleinhaus, 15 Am. Bankr. Inst. L. Rev. at 556. See also, for examples of the type of specificity required to satisfy applicable New York law, the discussion in U.S. Bank National Association v. South Side House, LLC, 2012 U.S. Dist. LEXIS, 10824, at *21-24, and In re LaGuardia Associates, L.P., 2012 Bankr. LEXIS 5612, at *14-16.

That type of specificity works notwithstanding the purpose of a make-whole, which is to ensure that the lender is compensated for being paid earlier than the original maturity of the loan for the interest it will not receive, because make-wholes are properly viewed as an option pursuant to which the parties have allocated the cost of prepayment between themselves. South Side House, 2012 U.S. Dist. LEXIS 10824, at *22-23; Northwestern Mutual Life Insurance Company v. Uniondale Realty Associates, 816 N.Y.S.2d at 984; Charles & Kleinhaus, 15 Am. Bankr. Inst. L. Rev. at 566-67. However, the option, as

noted, must be specific if the parties want it to apply even after acceleration of the debt.

The trustees for the first and 1.5 lien notes also contend that, even if they are not entitled to an Applicable Premium, other provisions of the indentures refer to a lower case “prepayment premium.” For example, as I noted, Section 3.02 of the indentures refers to the "Redemption of Notes at the election of the Issuer or otherwise as permitted or required by any provision of this Indenture shall be made in accordance with such provision in this Article." (Emphasis added.) (Although it should be noted that Section 3.09 of the indentures provides for a mandatory redemption, which is what the “or otherwise” reference in Section 3.02 apparently addresses.) In addition, they point out that Section 6.02 of the indentures provides for the automatic acceleration upon the debtors’ bankruptcy of “the principal of, premium, if any, and interest on all the Notes” (emphasis added), and Section 6.03 states that "If an Event of Default occurs and is continuing, subject to the terms of the New Intercreditor Agreement or the Junior Priority Intercreditor Agreements, the Trustee may pursue any available remedy at law or equity to collect the payment of principal of or interest on the Notes or to enforce the performance of any provision of the Notes, this Indenture or the Security Documents" (that is, acknowledging the trustees’ common law enforcement rights, which, the trustees,

contend, would include the payment of a prepayment premium).

Each of these references to other rights or “premiums, if any,” to be paid upon prepayment are not specific enough, however, to overcome the requirement of New York law that I have previously outlined in order for a make-whole or prepayment claim to be payable post-acceleration.

Moreover, the "if any" language that I’ve quoted refers back to the actual provisions of the indentures and notes, the only one of which that specifically provides for an optional redemption and payment of a specific premium (the Applicable Premium) does not sufficiently provide for payment after acceleration under New York law, as previously discussed. A similar provision appeared in the instrument at issue in In re LaGuardia Associates, L.P., 2012 Bankr. LEXIS 5612, and Judge Raslavich construed it much as I have here, stating, "On the contrary, [such provision] references ‘any payment required to be paid under the note.’ That returns the inquiry back to Section 1.02(b) of the note and its description of the specific two events which have not occurred.” Id. at *19-20. Similarly, Section 3.02 of the indentures, which states, "Redemption of Notes at the election of the Issuer or otherwise, as permitted or required by any provision of this Indenture, shall be made in accordance with such provision and this Article,” does not create a separate make-whole right enforceable upon acceleration of the debt but only refers to rights that may be

triggered in accordance with the specific provisions of Article 3.

It is also the case that Section 3.06 of the indentures, which states that "Once notice of redemption is delivered in accordance with Section 3.05, Notes called for redemption become due and payable on the redemption date and at the redemption price stated in the notice, except as provided in the final sentence of paragraph 5 of the Notes," is superseded by the automatic acceleration upon the issuer’s bankruptcy, provided for in Section 6.02. That is, the foregoing language from the Section 3.06 is not a substitute for acceleration, which made the notes due and payable on the bankruptcy petition date, or a clear enough statement that, notwithstanding acceleration, the redemption date, that is, the date upon which the issuer would call the notes for redemption, would artificially jump ahead of the prior acceleration or ignore the acceleration and entitle the holders to a make-whole under New York law.

Therefore, the indentures and notes do not overcome or satisfy the requirement under New York law that a make-whole be payable specifically notwithstanding acceleration or payment prior to the original maturity date under the terms of the parties’ agreements. There is, therefore, no claim for Applicable Premium or any other amount under the indentures and notes for the first and 1.5 lien holders that would be

triggered by the lien holders’ treatment under the debtors’ chapter 11 plan, or any other payment of their notes following their automatic acceleration under Section 6.02 of the indenture.

This leaves to be decided the first and 1.5 lien holders’ remaining claim based on payment, under the chapter 11 plan by new replacement notes, of the first and 1.5 notes prior to their maturity that would arise, they contend, under New York’s common law rule of perfect tender or, as argued by the trustees, under the first sentence of paragraph 5 of the notes. That sentence, they contend, sets forth a “non-call” covenant when it states, "Except as set forth in the following two paragraphs [which reference payments of contractual make-whole that I have just ruled are not here owing], the Note shall not be redeemable at the option of MPM prior to October 15, 2015."

The debtors and the second lien holders argue that this sentence is no more than an introduction or framing device for the notes’ elective redemption provisions in return for payment of the Applicable Premium, which immediately follow the “non-call” sentence, and is not a specific contractual non-call provision. In support of this contention, they point out that the make-whole right actually arises under Sections 3.01-3.03 of the indentures, which then reference paragraph 5 of the notes, which states the right to a make-whole amount under certain circumstances. They are right: the indentures and notes

do not contain a covenant stating the amount owing upon the voluntary call of the notes with the exception of sections 3.01-3.03 and the definition of Applicable Premium.

This leaves the trustees with the argument that New York's common law of perfect tender would apply even if their agreements were silent regarding the consequences of such prepayment. That is, the trustees for the first and 1.5 lien notes contend that the holders are entitled to a claim under New York law for a prepayment premium based merely on the fact of prepayment, which, they point out, would be preserved under the general reservation of common law rights and remedies set forth in Section 6.03 of the indentures.

As noted previously, New York law would, in fact, provide for such a claim for breach of the rule of perfect tender, at least one for specific performance. However, applying the two-step claim analysis required by Ogle v. Fidelity & Deposit Company of Maryland, 586 F.3d at 147-48, the trustees would not have an allowable claim for such damages under the Bankruptcy Code, because this is one of the few instances when specific provisions of the Bankruptcy Code disallow such a claim -- section 506(b), as well as section 502(b)(2), which disallows claims for unmatured interest.

First, it is well recognized that, notwithstanding New York's perfect tender rule, such right is not enforceable by specific performance in a bankruptcy case, given the Bankruptcy

Code's non-contractual acceleration of debt for claim determination purposes. See, for example, HSBC Bank USA v. Calpine Corp., 2010 U.S. Dist. LEXIS 96792, at *11-14, and Charles & Kleinhaus, 15 Am. Bankr. Inst. L. Rev. at 563-64.

In addition, as noted, no provision of the indentures and notes (except as already found to be inapplicable in light of the acceleration of the debt) provides for an additional premium to be paid upon the prepayment of the notes. Thus, the claim would not fall under the allowed claim provided to oversecured creditors for fees and charges under the parties' agreement under section 506(b) of the Bankruptcy Code up to the value of their collateral. See HSBC Bank USA v. Calpine Corp., 2010 U.S. Dist. LEXIS 96792, at *14-21; In re Solutia Inc., 379 B.R. at 485; In re Calpine Corp., 365 B.R. 392 (Bankr. S.D.N.Y. 2007), rev'd on other grounds, 2011 U.S. Dist. LEXIS 62100 (S.D.N.Y. June 7, 2011); and In re Vest Assocs., 217 B.R. 696, 699 (Bankr. S.D.N.Y. 1998).

It is not clear whether a claim for breach of a contractual make-whole provision should be viewed as a claim for unmatured interest (compare In re Trico Marine Services, Inc., 450 B.R. 474, 480-81 (Bankr. D. Del. 2013) (recognizing split of authority but holding that claim for breach of contractual make-whole is liquidated damages for breach of an option to prepay, not for unmatured interest), and In re Doctors Hospital of Hyde Park, Inc., 508 B.R. 596, 605-06

(Bankr. N.D. Ill. 2014) (claim for breach of contractual yield maintenance premium is for unmatured interest not paid as a result of prepayment). However, the measure of a claim based on New York's rule of perfect tender or a non-call right that does not provide for liquidated damages would be the difference between the present value of the interest to be paid under the first and 1.5 lien notes through their stated maturity and the present value of such interest under the replacement notes to be provided to the fist and 1.5 lien holders under the chapter 11 plan, which should equate to unmatured interest. See Charles & Kleinhaus, 15 Am. Bankr. Inst. L. Rev. at 541-42, 580-81. Accordingly such a claim also would be disallowed as unmatured interest under section 502(b)(2) of the Bankruptcy Code. It is not interest that has accrued during the bankruptcy case, but would, rather, accrue in the future, at least to 2015 if not to 2020, the original maturity date of the notes, and, therefore, would not be an allowed claim under section 502(b)(2). HSBC Bank USA v. Calpine Corp., 2010 U.S. Dist. LEXIS, at *14-21.

The two cases relied upon by the first and the 1.5 lien trustees for the contrary proposition actually are consistent with the foregoing analysis. The debtors in both cases (unlike here) were solvent and, therefore, the courts found them to be subject to an exception to section 502(b)(2) of the Code's disallowance of claims for unmatured interest

under either equitable principles, as set forth in the legislative history to section 1124 of the Bankruptcy Code (see 140 Cong. Rec. H 10,768 (October 4, 1994)), or because of the application of the best interests test in section 1129(a)(7) of the Code when the debtor is solvent. See In re Premier Entertainment Biloxi, LLC, 445 B.R. at 636-37; In re Chemtura Corp., 439 B.R. at 636-37.

This analysis applies also to any claim premised on the debtors' breach of the provision in the last sentence Section 6.02 of the indentures, obliquely referenced in paragraph 15 of the notes, that the issuer would under certain circumstances permit the rescission of automatic acceleration under Section 6.02 upon the issuer's bankruptcy. The damages for breach of such a rescission right, which are unspecified in both the indentures and the notes, would equate to the same lost unmatured interest that would apply to a breach of the right of perfect tender or non-liquidated damages non-call right.

Accordingly, I conclude both for purposes of confirmation of the debtors' chapter 11 plan, as well as for Adversary Proceeding Nos. 14-08227 and 14-08228, that the plain language of the first and 1.5 lien indentures and notes as applied to the present facts requires the allowed claim of the indenture trustees for the first and 1.5 lien holders to exclude any amount for Applicable Premium or any other damages

based on the early payment of the notes.

There is no relevant commentary or conduct by the parties that would or should change that view, given that there is no ability to consider parol evidence in light of the plain meaning of the agreements under the contract interpretation cases that I have already cited. I will note, however, that the trustees for the first and 1.5 lien holders have contended that the disclosure in the prospectuses for their notes, while lengthy, fails to highlight the risk that, upon bankruptcy and the automatic acceleration of the notes, no make-whole claim or other damages would be owed upon the early payment of the notes.

It is true that there is no such disclosure. I note, however, that the vast majority of risk disclosures in the prospectuses, 54 risk factors, pertains to fact-based risks -- either market or business or product risks. Of the risk factors disclosed, only six are bankruptcy-related, and they do not specifically disclose material risks affecting the notes in the issuer’s bankruptcy in addition to the risk to the make-whole claim. Two disclosed bankruptcy-related risks pertain to the potential avoidance of the notes or the liens under chapter 5 of the Bankruptcy Code. Others state that the ability of holders to realize upon their collateral and claims is subject to certain bankruptcy law limitations (which may, in fact, include, in broad scope, the risk that the first and 1.5 lien

holders may not have an allowed claim based on prepayment of the notes in a bankruptcy case, although perhaps such disclosure could simply be taken as a reference to the imposition of the automatic stay under section 362(a) of the Bankruptcy Code). But, as noted, there are other specific bankruptcy risks in addition to risks to the allowance of a make-whole claim that are not disclosed, including the risk of being crammed down with notes payable over time, as opposed to being paid in cash or reinstated, under section 1129(b)(2) of the Bankruptcy Code.

Moreover, as observed by the Court in South Side House, 2012 U.S. Dist. LEXIS 10824, at *12, the law that I have applied to the first and 1.5 lien holders' make-whole claim is "well-settled" and long established. It has been stated readily and cogently by courts that do not specialize in New York law; i.e., courts from the Seventh, Third, and Fifth Circuits, the latter two from Pennsylvania and Mississippi, as well as Delaware. Thus it does not appear, to the extent that one would even give any weight to the disclosure, or lack thereof, in the prospectuses, that the noteholders needed to be specially alerted to the risk that their make-whole claims might be disallowed in bankruptcy based on the automatic contractual acceleration of their notes, beyond the disclosure that the issuer's bankruptcy might alter the noteholders' rights.

Relatedly, as I’ve noted, the first and 1.5 lien trustees have sought freedom from the automatic stay under section 362(a) of the Bankruptcy Code to implement the rescission of the automatic acceleration of the notes that occurred under Section 6.02 of the indentures upon the debtors’ bankruptcy filing. The mechanism for such rescission is also set forth in Section 6.02 of the indentures and is loosely referenced in paragraph 15 of the notes, which states, "Under certain circumstances, the Holders of a majority in principal amount of the outstanding Notes may rescind any such acceleration with respect to the Notes and its consequences."

The first and 1.5 lien holders want to rescind the contractual acceleration under Section 6.02 to avoid the fatal effect of such acceleration upon their make-while rights in light of their agreements’ lack of the specificity required to trigger the Applicable Premium upon acceleration under New York law.

The trustees make three arguments to support their request. First, they state that the automatic stay does not actually apply to sending a rescission notice. Second, they contend that, even if the automatic stay under section 362(a) of the Code applies to such a notice, rescission is excepted from the stay by section 555 of the Bankruptcy Code. Finally, they contend that, even if the automatic stay applies, they

should be granted relief from the stay pursuant to section 362(d) of the Code.

I conclude that the automatic stay does, in fact, apply to the sending of a rescission notice and contractual deceleration of the debt. Two provisions of the Bankruptcy Code’s automatic stay apply here. First, section 362(a)(3) of the Code states that the automatic stay upon the filing of the case includes a stay of "any act to obtain possession of property of the estate or property from the estate or to exercise control over property of the estate." Section 362(a)(6) then states that the following also are stayed: "any act to collect, assess or recover a claim against the debtor that arose before the commencement of the case under this title."

In essence, as I've said, the first and 1.5 lien trustees seek through a rescission notice to exercise a right under the indentures, which, as contracts to which the debtors are a party, are property of the debtors’ estates. The purpose of sending a rescission notice would be to enable the holders to recover a sizeable claim against the debtors -- that is, to resurrect their make-whole claim, which has been loosely quantified as approximating $200 million -- through deceleration of the debt. They thus seek to control property of the estate by exercising a contract right to the estate’s detriment and recover, by decelerating, a claim against the

debtors.

The Second Circuit has recently held in a very similar context that sending such a notice would, in fact, be subject to the automatic stay of section 362(a). In re AMR Corp., 730 F.3d at 102-03 and 111-12, citing In re 48th Street Steakhouse, Inc., 835 F.3d, 427 (2d Cir. 1987), and In re Enron Corp., 300 B.R. 201 (Bankr. S.D.N.Y. 2013), in which contract rights were found to be property of the debtor and actions that had the effect of terminating, or would, in fact, terminate or alter, those rights, even if taken against a third party, as in 48th Street Steakhouse, would therefore constitute the exercise of control over property of the estate stayed by section 362(a)(3). See also In re Solutia Inc., 379 B.R. at 484-85.

Additionally, here, as in AMR and Solutia, the purpose of sending such a notice would be to recover a claim against the debtors, because the first and most important step in recovering a make-whole claim would be to resurrect the right to the Applicable Premium by decelerating the debt. Therefore, it is clear that the automatic stay under section 362(a)(6) of the Code also applies.

The trustees have argued that a rescission notice would not alter what the debtors would retain under the plan, and, therefore, that section 362(a)(3) should not apply, because this is fundamentally, or economically, an intercreditor dispute; i.e., the value -- the $200 million --

that the first and 1.5 lien holders seek to include as part of their claim if rescission and deceleration is permitted, would otherwise effectively be distributed to the second lien holders and the trade creditors under the plan.

However, that is not a proper reading of section 362(a) of the Bankruptcy Code. As noted by the court in In re Strata Title, LLC, 2013 Bankr. LEXIS 1704 at *17-18 (Bankr. D Az. Apr. 25, 2013), such a reading of section 362(a)(3) would add a phrase to the statute that is not present, namely "unless such act would provide economic value to the estate." Moreover, it ignores the applicability of section 362(a)(6).

This is also clearly not a case, as the trustees contended at oral argument, where the automatic stay wouldn't apply because the transaction is only between third parties, in the nature of a letter of credit draw which is not subject to the automatic stay because the issuer has a separate and independent obligation to the beneficiary the payment of which does not control the debtor’s property; rather, the effect on the debtors’ estates of the requested rescission and deceleration would be direct -- controlling and increasing the first and 1.5 lien holders’ recovery of property of the estate.

Similarly, Second Circuit cases cited by the trustees for the proposition that, "[t]he general policy behind section 362(a) is to grant complete immediate, albeit temporary, relief to the debtor from creditors and also to prevent dissipation of

the debtor's assets before any distribution to creditors can be effective," SEC v. Brennan, 230 F.3d 65, 70 (2d Cir. 2000), are taken entirely out of context, whereas the trustees ignore numerous cases, discussed below, in which the courts have prohibited, as did the Second Circuit in AMR, actions that would permanently alter, postpetition, the rights of creditors that existed on the petition date, such as by sending notices like the rescission notice at issue here.

It is clear that there is a difference between automatic acceleration pursuant to a contract, as is the case here, and acceleration generally as a matter of bankruptcy law upon the commencement of a bankruptcy case for the purpose of determining claims against the estate, as I'll discuss in more detail when I consider whether relief should be granted from the stay pursuant to section 362(d) of the Code. For present purposes, however, it is sufficient to note that here a contract to which the debtors are a party would specifically be affected for the purpose of recovering on a claim against the debtors, and, therefore, the automatic stay under section 362(a) of the Bankruptcy Code applies.

In addition, the indenture trustees make an argument that was not raised in AMR or Solutia: that the sending of a rescission notice to decelerate the first and 1.5 lien notes would merely be liquidating a securities contract, which is permissible under section 555 of the Bankruptcy Code

notwithstanding the automatic stay under section 362(a).

Section 555 of the Bankruptcy Code provides, "The exercise of a contractual right of a stockbroker, financial institution, financial participant or securities clearing agency to cause the liquidation, termination or acceleration of a securities contract as defined in section 741 of this title, because of a condition of the kind specified in section 365(e) of this title [i.e., so called “ipso facto” conditions such as the commencement of the bankruptcy case], shall not be stayed, avoided or otherwise limited by operation of any provision of this title."

The first and 1.5 lien trustees contend that the effect of the rescission notice would be to fix and, therefore, liquidate, the amount of their claims in the bankruptcy case and, therefore, that it would, pursuant to section 555 of the Code, not be subject to the automatic stay. There are several problems with this argument, however.

First, I have serious doubts that the indenture itself is a securities contract as defined in section 741(7)(A) of the Bankruptcy Code, at least with respect to this issue. Generally speaking, section 741(7) of the Code’s definition of “securities contract,” which is lengthy, states that it is a contract for the purchase, sale or loan of a security. Clearly, the indentures themselves are not contracts for the purchase, sale or loan of a security; they instead set forth

the terms under which the underlying notes will be governed and the role of the trustees in connection therewith. See In re Qimonda Richmond, LLC, 467 B.R. 318, 323 (Bankr. D. Del. 2012), holding, albeit without much discussion, that an indenture does not fall within the definition of section 741(7)(A).

The trustees rely on subsection (A)(x) of section 741(7) of the Code to fit the indentures within the “securities contract” definition notwithstanding that the indentures themselves are not contracts for the purchase, sale or loan of a security. Section 741(7)(A)(x) states, in relevant part, "A ‘securities contract’ means . . . (x) a master agreement that provides for an agreement or transaction referred to in [among other sub-clauses] clause (i) [that is, a contract for the purchase, sale, or loan of a security, among other transactions], without regard to whether the master agreement provides for an agreement or transaction that is not a securities contract under this subparagraph, except that such master agreement shall be considered to be a securities contract under this subparagraph only with respect to each agreement or transaction under such master agreement that is referred to in clause (i) [i.e., a contract for the purchase, sale or loan of a security]."

It is far from clear that the indentures would be viewed as such a master agreement, however, given the proviso in the last clause of subsection 741(A)(x), with respect to the

indentures’ rescission section, which does not itself pertain to the purchase, sale or loan of the notes and, further, because paragraph 15 of the notes does not specify any rescission right but instead refers to a right that is exercisable under unidentified provisions upon certain unspecified circumstances.

Relatedly, and even more significantly, I do not believe that sending the rescission notice, the consequences of which, as I have stated, would enable the deceleration of the notes to permit the increase of a claim against the debtors in the amount of the make-wholes, is in fact covered by section 555 of the Bankruptcy Code, because it is not a “liquidation” as contemplated by that section.

The customary interpretation of section 555 is that it "provides a tool for the non-defaulting. . .participant to exercise its contractual right to close-out, terminate or accelerate a ‘securities contract.’ Such a close-out or liquidation typically entails termination or cancellation of the contract, fixing of the damages suffered by the nondefaulting party based on market conditions at the time of liquidation, and accelerating the required payment date of the net amount of the remaining obligations and damages." In re American Home Mortgage, Inc., 379 B.R. 503, 513 (Bankr. D. Del 2008), quoting 5 Collier on Bankruptcy, paragraph 555.04 (16th ed. 2014)).

Here, to the contrary, the first and 1.5 lien trustees look to decelerate and create a different claim than existed on the bankruptcy petition date. As discussed by Judge Peck in decisions in the Lehman Brothers case pertaining to a closely analogues provision of the Bankruptcy Code, section 560, that type of action does not fall within section 555 of the Bankruptcy Code, which, with its companion sections, is a narrow provision that should not be used to improve a contract party's standing or claim in the bankruptcy case. See Lehman Brothers Special Fin. Inc. v. Ballyrock AGS CDO 2007-1 Ltd., 452 B.R. 31, 40 (Bankr. S.D.N.Y. 2011), in which Judge Peck held that, rather than exercising a right subject to the safe harbor of section 560 of the Code, the parties were impermissibly seeking to improve their positions. See also In re Lehman Brothers Holdings, Inc., 502 B.R. 383, 386 (Bankr. S.D.N.Y. 2013), discussing Ballyrock and Lehman Brothers Special Fin. Inc. v. BNY Corporate Trading Services Ltd., 422 B.R. 407, 421 (Bankr. S.D.N.Y. 2010).

Moreover, the rescission right sought to be exercised here is not a right automatically arising upon the commencement of the debtors’ bankruptcy case and, thus, covered by section 365(e) of the Bankruptcy Code as referenced in section 555. As noted, the trustees instead seek to decelerate debt that was automatically accelerated under Section 6.02 of the indentures upon the bankruptcy filing. Thus, the exercise of the

rescission right does not fall within the plain language of section 555 of the Code.

I have also concluded, in large measure based upon the AMR case, that relief from the automatic stay should not be granted here under section 362(d) of the Bankruptcy Code. The Second Circuit in AMR affirmed Judge Lane's determination in the exercise of his discretion not to lift the automatic stay to permit a similar notice to be sent. 730 F.3d at 111-12.

The trustees argue for stay relief under both sections 362(d)(1) and (d)(2) of the Code. I conclude that subsection (d)(2) is not applicable here. It provides for "relief from the stay provided under subsection (a) of this section with respect to a stay of an act against property under subsection (a) of this section if (A) the debtor does not have an equity in such property; and (B) such property is not necessary to an effective reorganization." Here, the debtors convincingly argued that subsection 362(d)(2) was intended to address, and does, by its terms, address, acts against property in which a creditor has an interest, such as a lien interest, as opposed to a right against a contract or to exercise a right under a contract, such as under Section 6.02 of the indentures. See In re Motors Liquidation Company, 2010 U.S. Dist. LEXIS 125182, at *8-9 (S.D.N.Y. Nov. 17, 2010).

Moreover, under section 362(g) of the Code, the movant has the burden to show that the debtor does not have an equity

in such property under section 362(d)(2)(A), and I believe that it was conceded during oral argument, and, in any event, I so find, that the first and 1.5 lien trustees have not sustained that burden. It is not clear to me how they possibly could have shown that the debtors have no equity in the indentures, given that, before a rescission the trustees' claims pursuant to the indentures are worth far less, perhaps $200 million less, than if the trustees obtain relief from the stay for rescission. That $200 million would establish, I believe, the debtors' equity in light of the fact that the trustees do not have a lien on or other prior interest in the indentures.

That leaves the trustee's request for relief under section 362(d)(1) of the Bankruptcy Code, which provides for relief from the automatic stay "for cause, including a lack of adequate protection of an interest in property of such party-in-interest." As noted, we are not dealing with a lien or other prior interest in property held by the indenture trustees; we are dealing with their desire to exercise a contract right, rescission. Therefore, the Second Circuit's Sonnax case, which applies generally where relief from the stay is sought for purposes other than to enforce an interest in property, controls. In re Sonnax Industries, 907 F.2d 1280, 1285-86 (2d Cir. 1990) (setting forth factors that may be relevant to a determination on a request to lift the automatic stay in such circumstances); see also In re Bogdanovich, 292

F.3d 104, 110 (2d Cir. 2002). AMR applied the Sonnax factors in this context. 730 F.3d at 111-12.

As I noted earlier, the sending of a rescission, or deceleration notice significantly impacts the debtors' estate and creditors -- in this case by enhancing claims potentially by hundreds of millions of dollars. It is, therefore, the type of action that courts have routinely refused to permit under section 362(d)(1) of the Bankruptcy Code. As noted by Judge Beatty in In re Solutia, 379 B.R. at 488, a contractual acceleration provision goes well beyond the acceleration that occurs as a matter of bankruptcy law with respect to the determination of claims against the estate. One can, as discussed in In re Solutia; In re Manville Forests Products Corp., 43 B.R. 293, 297-98 (Bankr. S.D.N.Y.) and HSBC Bank USA v. Calpine Corp., 2010 U.S. Dist. LEXIS 96792, at *10-11, observe that as a matter of law the filing of the bankruptcy case itself accelerates debt. However, a contractual acceleration provision advances the maturity date of the debt in ways that have consequences in the bankruptcy case beyond the operation of this general bankruptcy law principle. For example, such acceleration may give rise to a right to damages under section 1124(2)(C) of the Bankruptcy Code if the debtor later attempts to decelerate and reinstate the debt. It also may give the creditor a right to a different type or amount of interest; and the presence or absence of such a provision may

also affect rights against other parties including co-debtors. See, e.g., In re Texaco, Inc., 73 B.R. 960 (Bankr. S.D.N.Y. 1987). In that case, because there was no automatic contractual acceleration provision, noteholders sought to send an acceleration notice that would give them the right to an increased interest rate under their agreement. The court declined to lift the automatic stay. Id. at 968, stating that the noteholders sought more than simply to preserve the prepetition status quo. See also In re Metro Square, 1988 Bankr. LEXIS 2864, at *7-9 (Bankr. D. Minn., August 10, 1988). And, as noted, by Judge Lifland in In re Manville Forest Products, 43 B.R. at 298 n.5, “While the Court today holds that sending a notice of acceleration is unnecessary to file a claim against a debtor for the entire amount of the debt, despite the actual maturity date or the terms of the contract, this does not apply where notice is required as a condition precedent to establish other substantive contractual rights such as the right to receive a post-default interest rate. In that case, the sending of such notice would be ineffective under the automatic stay provisions of the Code if done without the provision of the bankruptcy court." Of course, Judge Lane performed a similar analysis in denying the trustee’s request for stay relief in In re AMR Corp., 485 B.R. 279, 295-96 (Bankr. S.D.N.Y. 2013), aff’d 730 F.2d at 111-12.

Thus, the first and 1.5 lien trustees’ request for

stay relief should not be granted to permit such a material change to be effectuated. Key “Sonnax factors” regarding the impact of rescission and deceleration on the parties and on the case strongly argue against granting such relief. Therefore, in the exercise of my discretion under section 362(d)(1) of the Code, I conclude that the automatic stay should not be lifted to enable the resurrection of a make-whole claim by means of the rescission of the automatic acceleration provided for in Section 6.02 of the indentures.

As previously noted, the holders of the first and 1.5 lien notes have voted as classes to reject confirmation of the debtors’ chapter 11 plan. The plan otherwise meets, as I've stated, the confirmation requirements of section 1129(a) of the Bankruptcy Code. But, to be confirmed over the objection of the objecting classes comprising the first and 1.5 lien holders, the plan must also satisfy the “cram down” requirements of section 1129(b) of the Bankruptcy Code. At issue is whether section 1129(b)(2) of the Code has been satisfied, there being no objection to the cramdown requirements pertaining to secured creditors set forth in section 1129(b)(1) with the exception of its requirement that the a plan be “fair and equitable,” which term is defined in section 1129(b)(2).

Section 1129(b)(2) of the Bankruptcy Code states, "For

the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements: (A) With respect to a class of secured claims, the plan provides -- (i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and (II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property." Section 1129(b)(2)(A)(ii) and (iii) set forth two other ways under which a plan can be “fair and equitable” to a dissenting secured class, but neither is applicable here, the debtors relying, instead, on section 1129(b)(2)(A)(i).

The only issue as to whether the debtors’ chapter 11 plan satisfies section 1129(b)(2)(A)(i) of the Code is whether the plan provides, as set forth in sub-clause (A)(i)(II), that the holders of the first and 1.5 lien notes will “receive on account of such claim deferred cash payments totaling the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property.” (Sub-clause (A)(i)(I) is satisfied because under the plan the first

and 1.5 lien holders shall retain the liens securing their claims to the extent of their allowed secured claims. Their liens are not being diminished under the plan, and, as I have previously found, those liens will secure the allowed amount of their claims.)

Whether the plan satisfies section 1129(b)(2)(A)(i)(II) of the Code depends on the proper present value interest rate under the replacement notes to be issued to the first and 1.5 lien holders under the plan on account of their allowed claims, given that those notes will satisfy their claims over seven and seven-and-a-half years, respectively. The debtors contend that the interest rates under the replacement notes are sufficient on a present value basis to meet the test of section 1129(b)(2)(A)(i)(II).

The interest rate on the new replacement first lien notes that are proposed to be issued under the plan is the seven-year Treasury note rate plus 1.5 percent. As of August 26, 2014, the date of my bench ruling, that would equal an approximately 3.60 percent interest rate, based on public data issued for such Treasury notes. The proposed replacement notes for the 1.5 lien holders would have an interest rate equal to an imputed seven-and-a-half-year Treasury note (based on the weighted averaging of the rates for seven-year and ten-year Treasury notes) plus 2 percent, which as of August 26, 2014 I calculated as approximately 4.09 percent based on public data

for such Treasury notes.

The indenture trustees for the first and the 1.5 lien holders contend that those rates do not satisfy the present value test in section 1129(b)(2)(A)(i)(II) of the Code and argue for higher interest rates under the replacement notes based on their view of what market-based lenders would expect for new notes if the same tenor issued by comparable borrowers.

The Court clearly is not writing on a blank slate on this issue. It is largely governed by the principles enunciated by the plurality opinion in Till v. SCS Credit Corp., 541 U.S. 465 (2004), and, to the extent that the Court has any concerns based on Till being a plurality opinion, In re Valenti, 105 F.3d 55 (2d Cir. 1997).

Both of those cases analyzed and applied a closely analogous provision in chapter 13 of the Bankruptcy Code, section 1325(a)(5)(B)(i)(II), which states that, among other things required to confirm a plan with respect to an allowed secured claim, the plan must provide that, "the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim." As noted by the Court in Till, this provision is not only closely analogous to other provisions of the Bankruptcy Code (including section 1129(b)(2)(A)(i)(II) that I have just quoted), but also "Congress likely intended bankruptcy judges and trustees to

follow essentially the same approach when choosing an appropriate interest rate under any of the many Code provisions requiring a court to discount a stream of deferred payments back to their present dollar value." 541 U.S. at 474. Valenti, which was cited favorably in Till and which applies generally the same approach as Till to the proper present value interest rate for chapter 13 plan purposes, has also been construed as applying in a chapter 11 context to the cramdown of a secured creditor under section 1129(b)(2)(A)(i)(II). In re Marfin Ready Mix Corp., 220 B.R. 148, 158 (Bankr. E.D.N.Y. 1998). As discussed later, there is no sufficiently contrary basis to distinguish the chapter 13 and chapter 11 plan contexts in light of the similarity of the language of the two provisions and the underlying present value concept that Till recognized should be applied uniformly throughout the Code.

Till and Valenti establish key first principles that I should follow, therefore, when considering the proper interest rate to present value a secured creditor’s deferred distributions under a plan for cramdown purposes. Both cases quite clearly rejected alternatives that were proposed, and have been proposed now by the first and 1.5 lien trustees, that require a market-based analysis or inquiry into interest rates for similar loans in the marketplace. That is, both cases rejected the so-called “forced loan” or “coerced loan” approach, which Valenti defined as adopting the "interest rate

on the rate that the creditor charges for loans of similar character, amount, and duration to debtors in the same geographic region." 105 F.3d at 63. See Till, 541 U.S. at 477, where the Court rejected market-based methodologies in favor of the so-called "formula approach":

> [We] reject the coerced loan, presumptive contract rate, and cost of funds approaches. Each of these approaches is complicated, imposes significant evidentiary costs, and aims to make each individual creditor whole rather than to ensure the debtor's payments have the required present value. For example, the coerced loan approach requires bankruptcy courts to consider evidence about the market for comparable loans to similar (though nonbankrupt) debtors -- an inquiry far removed from such courts' usual task of evaluating debtors' financial circumstances and the feasibility of their debt adjustment plans. In addition, the approach overcompensates creditors because the market lending rate must be high enough to cover factors, like lenders' transaction costs and overall profits, that are no longer relevant in the context of court-administered and court-supervised cramdown loans.

541 U.S. at 477. See also In re Valenti, 105 f.3d at 63-4, (rejecting forced loan approach in favor of a formula approach). Of course the so-called "presumptive contract rate,"

that Till rejected was also a market-based test based on the parties’ prepetition interest rate as adjusted for current market factors, as, in lesser degree, was the “cost of funds” approach that Till also rejected, which was based on the creditor’s cost of capital, again tracking a market, although, in that case, with the emphasis on the creditor’s characteristics rather than the debtor’s.

Both courts stated similar reasons for rejecting market-based approaches in setting a cramdown rate. As stated in Valenti, "the 'forced loan' approach misapprehends the 'present value' function of the interest rate. The objective of Section 1325(a)(5)(B)(ii) is to put the creditor in the same economic position it would have been in had it received the value of its allowed claim immediately. The purpose is not to put the creditor in the same position that it would have been in had it arranged a 'new' loan.” (Emphasis in the original). 105 F.3d at 63-4. "Moreover, as our analysis in the preceding section illustrates, the value of a creditor's allowed claim does not include any degree of profit. There is no reason, therefore, that the interest rate should account for profit." Id. at 64. Similarly, Till distinguished the cramdown rate from market loans; the former does not require the lender to be indifferent compared to the result in a foreclosure, where the creditor could then re-lend the proceeds in the marketplace, 541 U.S. at 476 , and should not “overcompensate[] creditors

because the market lending rate must be high enough to cover factors, like lenders' transaction costs and overall profits, that are no longer relevant in the context of court-administered and court-supervised cramdown loans." Id. 541 U.S. at 477-78.

The cramdown rate analysis, therefore, should focus on a rate that does not take market factors into account but, rather, starts with the riskless rate applicable to all obligations to be paid over time, adjusted for the risks unique to the debtor in actually completing such payment. Id. 541 U.S. at 474-80. It should thus be a relatively simple, uniform approach consistent with bankruptcy "courts' usual task of evaluating the feasibility of their debt adjustment plans" not on costly and expensive evidentiary hearings to discern marketplace data. Id. 541 U.S. at 477; see also In re Valenti, 105 F.3d at 64.

As noted, in light of the foregoing considerations the Supreme Court adopted, as did the Second Circuit in Valenti before it, a formula approach, which is also the approach adopted by the debtors (in contrast to the trustees for the first and 1.5 lien holders, who have utilized a market-based approach) with respect to the replacement notes to be issued under the plan. Under the formula approach, the proper rate for secured lenders' cramdown notes begins with a risk-free base rate, such as the prime rate used in Till, or the Treasury rate

used in Valenti, which is then adjusted by a percentage reflecting a risk factor based on the circumstances of the debtor's estate, the nature of the collateral security and the terms of the cramdown note itself, and the duration and feasibility of the plan. Till, 541 U.S. at 479; Valenti, 104 F.3d at 64. Both Till and Valenti held that, generally speaking, the foregoing risk adjustment should be between 1 and 3 percent above the risk-free base rate. Id.

It is clear from those opinions that the formula approach's risk adjustment is not a back door to applying a market rate. Indeed, the Supreme Court stated, "We note that if the Court could somehow be certain a debtor would complete his plan, the prime rate would be adequate to compensate any secured creditors forced to accept cramdown loans." 541 U.S. at 479 n.18. That is, no adjustment whatsoever to the risk-free rate would be required if the Court found that the debtors were certain to perform their obligations under the replacement notes. The focus, therefore, should be generally on the risk posed by the debtor within a specified band, as opposed to market rates charged to comparable companies. Nothing could be clearer than the two Courts' statements on that point. Therefore, as a first principle, the cramdown interest rate, under section 1129(b)(2)(A)(i)(II) of the Code, should not contain any profit or cost element, which were rejected by Till and the Second Circuit in Valenti as inconsistent with the

present-value approach for cramdown purposes. In addition, market-based evidence should not be considered, except, arguably and, if so secondarily, when setting a proper risk premium in the formula approach taken by Till and Valenti.

Notwithstanding this very clear guidance, some courts, and the first and 1.5 lien trustees here, have argued that a market rate test should nevertheless be followed in chapter 11 cases. They have relied, as they must since there is no other basis in Till or Valenti for the argument, entirely on footnote 14 in Till, which appears at 541 U.S. 476.

That footnote states, "This fact helps to explain why there is no readily apparent Chapter 13 cramdown market rate of interest. Because every cramdown loan is imposed by a court over the objection of a secured creditor, there is no free market of willing cramdown lenders. Interestingly, the same is <u>not</u> true in the Chapter 11 context, as numerous lenders advertise financing for Chapter 11 debtors-in-possession." (Emphasis in the original.)

Till's footnote 14 then cites certain web site addresses that advertise such financing, and continues, "Thus, when picking a cramdown rate in a Chapter 11 case, it might make sense to ask what rate an efficient market would produce. In the Chapter 13 context, by contrast, the absence of any such market obligates courts to look to first principles and ask only what rate will fairly compensate a creditor for its

exposure."

I have the following reactions to that discussion. First, as is clear from its introductory clause, Till’s footnote 14 is referring to a specific fact alluded to in the sentence to which it is footnoted, which is that the cramdown rate of interest does not “require that the creditors be made subjectively indifferent between present foreclosure and future payment,” that is, between future payment under the plan and how the creditor would put its money to use lending to similar borrowers after a foreclosure in the marketplace. Id. And then the Court says, "Indeed the very idea of a cramdown loan <u>precludes</u> the latter result: By definition, a creditor forced to accept such a loan would prefer instead to foreclose." (Emphasis in the original.) Therefore, footnote 14’s statement that "this fact helps to explain why there is no readily apparent Chapter 13 cramdown market rate of interest," is referring to a willingness to lend to a debtor in bankruptcy but does so in a context that very clearly rejects the lender’s right or to be rendered indifferent to cramdown or to be compensated for cramdown purposes on a market basis. More specifically, footnote 14 refers to debtor-in-possession financing, where third parties seek to lend money to a debtor and the debtor seeks to borrow it, in contrast to opposing the debtor’s forced cramdown “loan.”

(As an aside, I should note that Till has been

criticized for its understanding of debtor-in-possession, or "DIP" loans, and I believe no case has suggested that a DIP loan rate should be used as the rate for a cramdown present-value calculation. The criticism is found in 7 Collier on Bankruptcy, paragraph 1129.05[c][i] (16th ed. 2014), where the editors state, "The problem with this suggestion" -- i.e., footnote 14's reference to DIP loans -- "is that the relevant market for involuntary loans in Chapter 11 may be just as illusory as in Chapter 13. The reason for this illusion is the inapt and unstated inference the Court makes with respect to the similarity between the interest rates applicable to debtor-in-possession financing and the interest rates applicable to loans imposed upon dissenting creditors at cramdown. While both types of financing can occur in a Chapter 11 case, that may be the extent of their similarity. Debtor-in-possession financing occurs at the very beginning of the case, while the determination of a cramdown rate, under Section 1129(b)(2), occurs at confirmation. Thus, instead of the interim and inherently more uncertain risk present in debtor-in-possession financing, the court, at confirmation, is presented with a less risky, more stable and restructured debtor. The fact that the debtor is more stable is bound up in the court's necessary feasibility determination under Section 1129(a)(11). In addition, common risk factors, such as the loan's term and the level of court supervision, differ greatly between the two

types of financing. There are many more differences, but they can be summed up as follows: loans imposed at confirmation resemble more traditional exit or long-term financing than interim debtor-in-possession financing.”)

Thus it was not general financing in the marketplace that Till was focusing on in footnote 14, because, again, it was describing loans that lenders <u>want</u> to make to the debtor itself, not loans that they could make with the proceeds of a foreclosure or in the marketplace to similarly situated borrowers. This is made clear by footnote 15 in Till, as well as footnote 18 that I previously quoted. Footnote 15 states that the Court disagrees with the district court's coerced loan approach, which “aims to set the cramdown interest rate at the level the creditor could obtain from new loans of comparable duration and risk.” 541 U.S. at 477 n.15. Moreover, as noted before, the Court actually contemplated, in footnote 18, literally no premium on top of the risk-free rate if it could be determined with certainty that the debtor would complete the plan. Id. 541 U.S. at 479 n.18.

In addition, there clearly was some form of market for automobile loans to debtors like the debtors in the Till case. That market, in fact, had a lot of data behind it. Id. 541 U.S. at 481-82; 495 n.3 (dissenting opinion). Nevertheless, the Court felt constrained to refer to it as not a “perfectly competitive market,” Id. 541 U.S. at 481, for which Justice

Scalia's dissent somewhat berated the plurality. Id. 541 U.S. at 494-95. Indeed, based on my experience reviewing hundreds, if not thousands, of reaffirmation agreements and other matters involving auto loans, there are and always have been active markets for such loans, just as the value of cars and trucks is tracked in readily accessible market guides. Put differently, there are far more lenders and borrowers for auto loans, with access to more public data, than lenders and borrowers with respect to DIP or exit financing in chapter 11 cases. In this case, for example, the evidence shows that there were only three available exit lenders to the debtors, who eventually combined on proposed backup takeout facilities while seeking to keep confidential their fees and rate flex provisions.

This reality, as well as the fact that the plurality in Till felt the need discount less than a "perfectly competitive market," underscores, along with the rest of the opinion, that footnote 14 is a very slim reed indeed on which to require a market-based approach in contrast to every other aspect of Till. Certainly there is no meaningful difference between the chapter 11, corporate context and the chapter 13, consumer context to counter Till's guidance that courts should apply the same approach wherever a present value stream of payments is required to be discounted under the Code. Id. 541 U.S. at 474. The rights of secured lenders to consumers and secured lenders to corporations are not distinguished in Till,

nor should they be. Nor does the relative size of the loan or the value of the collateral matter under Till's footnote 14, as it should not. Till does state that a chapter 13 trustee supervises the debtor's performance of his or her plan, id. 541 U.S. at 477; however, with replacement notes overseen by an indenture trustee for sophisticated holders, there will at least be comparable supervision under the debtors' plan, particularly in a district like this where secured claims often are paid "outside" of chapter 13 plans and, therefore, the chapter 13 trustee will not know whether the debtor has defaulted on the secured debt post-confirmation.

In sum, then, footnote 14 should not be read in a way contrary to Till and Valenti's first principles, which are, instead of applying a market-based approach, a present value cramdown approach using an interest rate that takes the profit out, takes the fees out, and compensates the creditor under a formula starting with a base rate that is essentially riskless, plus up to a 1 to 3 percent additional risk premium, if any, at least as against the prime rate, for the debtor's own unique risks in completing its plan payments coming out of bankruptcy.

As I've stated, certain courts, nevertheless, have required a two-step approach, that is, first inquiring whether there is an efficient market, not for DIP loans, but for financing generally for borrowers like the debtor, and only if there is no such market, applying the formula approach as set

forth in Till and Valenti.

The leading case taking this approach is In re American HomePatient, Inc., 420 F.3d 559 (6th Cir. 2005), cert. denied, 549 U.S. 942 (2006). It is clear from that case, however, that prior to Till the Sixth Circuit, in contrast to the Second Circuit, had applied the coerced-loan method, id. at 565-66, and then concluded that, given that Till was not on all fours, it should continue to apply the coerced-loan approach unless there was no efficient market. Id. at **568.** This is, of course, in contrast to this Court's duty to follow the guidance offered by Valenti, as well as Till.

Other courts applying American HomePatient's two-step approach include Mercury Capital Corp. v. Milford Connecticut Associates, L.P., 354 B.R. 1, 11-2 (D. Conn. 2006) (remanding to the bankruptcy court to make an efficient market rate analysis); In re 20 Bayard Views LLC, 445 B.R. 83 (Bankr. E.D.N.Y. 2011) (undertaking, after an eleven-day trial, a market analysis before concluding that there was no efficient market for Till purposes, and then applying the Till formula approach); and In re Cantwell, 336 B.R. 688, 692-93 (Bankr. D. N.J. 2006) (applying Till formula approach in the absence of "an efficient market").

I conclude that such a two-step method, generally speaking, misinterprets Till and Valenti and the purpose of section 1129(b)(2)(A)(i)(II) of the Code based on the clear

guidance of those precedents.

Further, as noted by the Fifth Circuit in In re Texas Grand Prairie Hotel Realty, L.L.C., 710 F.3d 324 (5th Cir. 2013), the first step of the two-step approach is almost, if not always, a dead end. As that decision observed, the vast majority of cases have ultimately applied a Till prime-plus approach or base rate-plus approach to the chapter 11 cramdown rate, either having spent considerable time determining that there is no efficient market or simply by moving to the base-rate-plus formula in the first instance. Id. at 333-34 (citing cases). This should not be surprising because it is highly unlikely that there will ever be an efficient market that does not include a profit element, fees and costs, thereby violating Till and Valenti's first principles, since capturing profit, fees and costs is the marketplace lender's reason for being. That is, as acknowledged by counsel for the trustees in oral argument, market lenders need to be rewarded, or to receive a profit. (Moreover, the two-step approach has a perverse underpinning: if the debtor is healthy enough to correspond to borrowers who could receive comparable loans in the marketplace, it would in all likelihood have to pay a higher cramdown rate than under the Till and Valenti formula approach for debtors who could not obtain a comparable loan in the market.)

The indenture trustees nevertheless argue that the

debtors' case is unique, or at least highly unusual, in that the debtors have substantially contemporaneously with confirmation obtained backup loan commitments to fund the cash-out alternative if the first lien and 1.5 lien holder classes had voted to accept the plan. Specifically the debtors obtained commitments for a $1 billion first lien backup takeout facility and a bridge facility of $250 million. Those commitments provide for higher rates than the replacement notes under the plan for the first and the 1.5 lien holders.

For the committed first lien backup takeout facility, the rate is LIBOR plus 4 percent, with a floor for LIBOR of 1 percent. Because LIBOR is, at this time, approximately .15 percent, effectively this would be a five percent rate. (There is also an alternative base rate for this facility that, given today's prime rate of approximately 3.25 percent, would be 6.25 percent, which is, however, exercisable at the debtors' option.) The committed bridge facility provides for a rate of LIBOR plus 6 percent, increasing in .5 percent increments every three months, to a capped amount. It appears relatively clear that the debtors intend, if rates remain low, to take out that facility before it increases precipitously.

The trustees have argued that these backup takeout loans should be viewed as proxies for the Till formula rate, even though -- or, according to the trustees, because -- they are based on a market process, albeit one, as discussed above

that was relatively opaque and involved only three lenders who ultimately combined to provide the commitments on a semi-confidential basis.

Again, however, I believe that the trustees are misreading Till and Valenti in their emphasis on the market. In addition, it is clear to me that no private lender, including the lenders who the debtors have obtained backup takeout commitments from, would lend without a built-in profit element, let alone recovery for costs and fees, which also, as discussed above, is contrary to Till and Valenti's first principles and the purpose of section 1129(b)(2)(A)(i)(II).

The indenture trustees state that I should assume that all of the back-up lenders' profit is subsumed in the upfront fees that are to be charged under the agreements, as well as an availability fee, but they have not offered any evidence or rationale for that proposition I decline to assume that there is no profit element in the backup facilities' rates. The trustee also have offered no evidence of any profit element that could be backed out of the back-up loans. Therefore, I'm left with the conclusion that there is, in fact, a profit element which is unspecified and unquantified in the backup loans, which, therefore, makes these two loans, even if I were to accept a market-based approach, at odds with Till and Valenti, as well as the courts that have followed Till in the absence of any clear market for coercive loans and those courts

that have that followed Till or Valenti in a chapter 11 context without considering markets at all, including In re Village at Camp Bowie I LP, 454 B.R. 702, 712-13 (Bankr. N.D. Tex. 2011); In re SW Boston Hotel Venture, LLC, 460 B.R. 38, 56 (Bankr. D. Mass. 2011); In re Lilo Props., LLC, 2011 Bankr. LEXIS 4407, at *3-6 (Bankr. D. Vt. Nov. 4, 2011); and In re Marfin Ready Mix Corp., 220 B.R. at 158.

I conclude, therefore, that Till and Valenti's formula approach is appropriate here, that is, that the debtors are correct in setting the interest rates on the first and 1.5 lien replacement notes premised on a base rate that is riskless, or as close to riskless as possible, plus a risk premium in the range of 1 to 3 percent, if at all, depending on the Court's assessment of the debtors' ability to fully perform the replacement notes.

The first and 1.5 lien trustees have next challenged the debtors' analysis of the risk premium. As noted, that risk premium for the first lien replacement notes is 1.5 percent on top of the seven-year Treasury note rate, and with respect to the replacement notes for the 1.5 lien holders, it is 2 percent on top of an imputed seven-and-one-half-year Treasury note rate. I believe that, in light of the factors to be considered when deciding the proper risk premium under the Till and Valenti formula approach, namely, the circumstances of the debtors' estate, the nature of the security (both the

underlying collateral and the terms of the new notes), and the duration and feasibility of the reorganization plan, the debtors have also performed a proper analysis of the risk premium.

The record on this issue consists primarily of the declaration and testimony of Mr. Carter (the debtor’s CFO), the the expert reports and testimony of Mr. Derrough (the debtors’ investment banker), and the expert reports and testimony of Mr. Augustine (the first lien trustee’s investment banker) and the expert reports of Mr. Kearns (the 1.5 lien trustee’s investment banker).

The only meaningful analysis of the debtors' underlying economic condition and the only projections were those undertaken by the debtors in the process testified to by Mr. Carter and Mr. Derrough. I conclude that such analysis and projections resulted from a rigorous process based upon the debtors' bottoms-up, as well as top-down, budgeting activity for 2014, as well as the debtors’ actual results for 2013. The process benefitted, I believe substantially, from the input not only of Mr. Derrough and his team at Moelis, but also from testing by the debtors' future shareholders, including the members of the ad hoc committee of second lien holders and Apollo, who have committed, with others, to invest $600 million of equity in the reorganized debtors under the plan, in addition to agreeing to receive only equity on account of their

notes.

Although there was considerable kibbitzing by Messrs. Augustine and Kearns regarding the debtors’ projections, they engaged in no independent testing of them. Nor did they engage in a rigorous testing of those projections other than to point out that in the past eight of nine years the debtors have missed their projections, sometimes materially. Those eight or nine years of projections did not have the benefit of vetting by Moelis and the second lien holders, however, that I have discussed. Nor have Messrs. Augustine and Kearns conducted a valuation of the collateral or of the debtors as a going concern, accepting, essentially, the debtors’ valuations.

In addition, it was pointed out that the debtors have missed their projections for the first quarter of this case, where there was input from, I can assume, independent third parties interested in making sure the projections were accurate. However, I found credible Mr. Carter's testimony on this point (as I found Mr. Carter generally credible), which was that those downward results for the post-bankruptcy period were largely attributable to the effects of the bankruptcy case, which would be ameliorated if not ended by the debtors' emergence from bankruptcy and re-regularization of customer and supplier relationships.

As far as the analysis is concerned, the post-bankruptcy collateral coverage for the first and 1.5 lien

replacement notes is substantially better than the coverage in the Till case. Even with a twenty percent variance for each of the five years of the debtors' projections, it appears clear that the replacement notes would be repaid in full, particularly given the fact that I have found that there will be no make-whole amount included in the principal amount of the loans. Here, the first and 1.5 lien holders' new collateral coverage, unlike in Till (where it was one-to-one, the debt equaling the current value of the collateral, 541 U.S. at 470), and unlike in In re 20 Bayard Views (where it also was one-to-one with considerable execution risk, 445 B.R. at 112), has a large cushion. Here, the debt under the replacement notes is approximately 50 to 75 percent less than the value of the collateral therefor, and closer to 50 percent than 75 percent. Gross debt leverage also will substantially decrease under the plan, from 17.8 percent to 5.6 percent, or from $4.4 billion in debt down to $1.3 billion.

In light of those considerations, as well as the telling fact that there is a committed $600 million equity investment under the plan, one can assume that, in the nature of risk for debtors emerging from bankruptcy, the 1.5 and 2 percent factors chosen by the debtors are appropriate.

In response, the first and 1.5 lien trustees have not carried their burden to show why those risk premiums are too low. First, in proposing their alternative risk premiums their

experts have focused on market data, again, which includes a profit element.

In addition, they have not, as discussed above, effectively challenged the debtors' projections or valuations. They have pointed out the debtors' own disclosure of the risk that they may lose some senior management upon confirmation of the plan, although I assume that this risk was taken into account in the debtors' projections and is, with all respect to Mr. Carter and the other senior management team at the financial level, less likely to occur for truly senior management at the operational level, who might be harder to replace.

In addition, it appears that both Messrs. Augustine and Kearns have slanted their analysis in ways that undercut their opinions. Mr. Augustine has not provided any analysis about collateral coverage for the replacement notes or total enterprise value. He also added extra interest into his projections, in essence double counting, to set a gross debt leverage amount that would then justify the extra interest. He also appears to have picked the very high end of leverage and rate factors when stating that the market has, in the last two months, materially changed, while these factors have since adjusted downward (at least as of the confirmation hearing), and has ignored the fact that the reorganized debtors' leverage continually goes down under the debtors' projections, including

under the twenty percent per year down-side projection scenario that Mr. Derrough ran, instead taking, in effect, a one-time leverage snapshot at its peak.

Mr. Kearns, although not taking as many liberties as Mr. Augustine, only focused on collateral leverage while ignoring the $600 million equity investment and total debt leverage.

Both experts for the first and 1.5 lien trustees also referred to rates of default for notes on a market basis that are rated, as they believe the replacement notes would be rated, at B2B or B and referred to defaults of, in Mr. Kearns' case, 34 percent in respect of such securities. They did not analyze, however, the difference between default and recovery rates. Clearly, the risk of default is an important risk to consider in this type of analysis, but the more important risk is the ultimate risk of non-payment (for example, notwithstanding the debtors’ bankruptcy, there is sufficient committed backup takeout financing to pay the first and 1.5 lien holders’ allowed claims in full in cash), which is where collateral coverage and total debt leverage come into play and support the debtors’ analysis.

The experts for the first and 1.5 lien trustees have also complained about the duration of the notes, although the first lien replacement note’s seven-year term is, in essence, the remaining term of the present first lien notes, and the

risk differential attributable to the 1.5 lien replacement notes’ seven-and-a-half year maturity in Mr. Kearns' chart is de minimis.

I also believe that once one takes out fees such as pre-payment fees and other costs and similar covenants, the covenants in the replacement notes for the first and the 1.5 lien holders are not materially different on an economic basis from the covenants in the proposed backup takeout facilities.

Consequently, applying a formula of prime plus 1 to 3 percent, as I believe is appropriate under Till and Valenti unless there are extreme risks that I believe do not exist here, a risk premium of 1.5 and 2 percent, respectively, for the two series of replacement notes is appropriate.

There is one point, however, on which I disagree with the debtors' analysis. The debtors, consistent with Valenti, 105 F.3d at 64, and the well-reasoned Village at Camp Bowie case, 454 B.R. at 712-15, chose as their base rate the applicable or imputed Treasury note rate. It was appropriate for them to do this, rather than blindly following the prime rate used in Till. The Treasury note rate actually is, as both Mr. Kearns and Mr. Derrough testified, often used as a base rate for longer-term corporate debt such as the replacement notes. The prime rate may, on the other hand, be a more appropriate base rate for consumers, although Valenti chose the Treasury rate, instead, perhaps because such loans are

considered to be essentially riskless. Both rates of course are easily determinable. But the Treasury rate, as confirmed by all three experts, does not include <u>any</u> risk, given that the United States government is the obligor, whereas an element of risk is inherent in the prime rate, which strongly correlates to the interest rate banks charge each other on overnight interbank loans and thus may reflect risks seen in banks' financial strength, of stronger concern during the last few years.

Given that fact, I question whether the 1 to 3 percent risk premium spread over prime used in Till would be the same if instead, as here, a base rate equal to the Treasury were used. I say this in particular under the present circumstances where the prime rate for short-term loans is materially higher than the Treasury rate for long-term loans, a somewhat anomalous result. It seems to me, then, that although the general risk factor analysis conducted by Mr. Derrough was appropriate, there should be an additional amount added to the risk premium in light of the fact that the debtors used Treasury rates as the base rate. The additional increment, I believe, should be another .5 percent for the first lien replacement notes, and an additional .75 percent for the 1.5 lien replacement notes. I believe that these adjustments adequately take into account risks inherent in the debtors' performance of the replacement notes above the essentially

risk-free Treasury note base rates. Therefore, rather than being the seven-year Treasury plus 1.5 percent, equaling 3.6 as of August 26, 2014, the rate for the first lien replacement notes should be the Treasury rate plus 2 percent, for an overall rate of 4.1 percent as of such date; and the rate for the 1.5 lien replacement notes should be the imputed seven-and-a-half-year Treasury note rate plus 2.75 percent, or a 4.85 rate as of August 26, 2014. This would require an amendment to the plan, obviously, and I don't know whether the necessary parties would agree to it, but I believe that they should, because it is necessary to cram down the plan over the objection of the first and 1.5 lien holder classes.

That leaves one remaining issue, which is the confirmability of the plan in light of the plan’s third-party release and injunction provisions. Those provisions have not been objected to except for the first and 1.5 lien trustees’ objection to the inclusion of third-party releases for parties named or identified in state court lawsuits brought by the first and 1.5 lien trustees to enforce the terms of the Intercredtor Agreement on the second lien holders. (Those lawsuits have been removed to this Court, although remand motions are pending.) The second lien holder third parties covered by the plan’s release and injunction provisions are referred to here as the “Released Second Lienholders”).

While it is true that third-party releases and related injunctions in Chapter 11 plans and confirmation orders are, under the law of the Second Circuit, proper only in rare cases, see Deutsche Bank AG v. Metromedia Fiber Network, Inc., 416 F.3d 136, 141 (2d Cir. 2005), if they are consensual or are not objected to after proper notice, courts generally approve them unless they are truly overreaching on their face. I do not find anything truly offensive in these releases and, thus, to the extent that they have not been objected to or a party voted in favor of the plan or did not opt out notwithstanding the clear notice in the ballot that stated, in upper-case letters, "If you voted to reject the plan and you did not opt out of the release provisions by checking the box below, or if you voted to accept the plan regardless of whether you checked the box below, you will be deemed to have conclusively, absolutely, unconditionally, irrevocably and forever released and discharged the Released Parties from any and all claims and causes of action to the extent provided in Section 12.5 of the plan," the plan may be confirmed consistent with both Metromedia and the case law interpreting it, as summarized by Judge Lane in In re Genco Shipping & Trading, Ltd., 513 B.R. 233 (Bankr. S.D.N.Y. 2014).

It is another story, however, where there is a substantial objection to a third-party release and related injunction, which is the case here, albeit that it is by a

group that at least under the ruling that I just gave, would be satisfied as a matter of law by a plan that would be consistent with my cramdown ruling (which is one of the factors arguing for a release’s effectiveness under the caselaw that I have cited).

Here, what was originally sought to be released included claims made by the first and 1.5 lien trustees against the Released Second Lienholders in the litigation that has been removed to this Court. In that litigation, the first and 1.5 lien trustees assert a breach claim under the Intercreditor Agreement based on the Released Second Lienholders’ support of the plan and receipt of consideration under the plan before the payment to the holders of the first and 1.5 liens required by the Intercreditor Agreement, which, they contend, under the agreement’s definition of "discharge of indebtedness,” is payment in full, in cash.

In light of comments made during the confirmation hearing regarding my concerns about the proposed release as it applied to the Released Second Lienholders, the debtors and those released parties have agreed, however, to amend the plan to carve out of the release of rights with respect to, and the discharge of, the pending litigation, provided that the Court maintains jurisdiction over that litigation.

I conclude, having evaluated the factors under Metromedia and the case law supporting third-party plan

releases -- and, though not fully, having reviewed the litigation claims against the Released Second Lienholders -- that this modified release is appropriate and would be sustained if the plan were otherwise confirmable.

It is is clearly the case that the Released Second Lienholders are providing substantial consideration under the plan. They are agreeing not to seek pari passu treatment on their deficiency claims with the trade creditors (that is, all creditors with unsecured claims with the exception of the senior subordinated unsecured noteholders), who are being paid in full under the plan.

They are also committing to underwrite the $600 million equity investment under the plan. They have also supported confirmation of the plan starting with executing a prepetition plan support agreement (although I agree with Judge Lane’s conclusion in Genco Shipping & Trading that one cannot bootstrap a plan support agreement containing an indemnification right into consideration for a third-party release under a plan).

I also believe that the third-party release is an important feature of this plan. Counsel for the indenture trustees, in essence, asked me to play a game of chicken with the Released Second Lienholders (beyond my comments that led to the on-the-record amendment of the release) to see if they actually would withdraw their support of the plan if the plan

and confirmation order were not reasonably satisfactory to them, by requiring the full deletion of the release, but I'm not prepared to do that. I believe that, instead, I can assess the likelihood that the Released Second Lienholders would walk as well as Mr. Carter on behalf of the debtors did, and assume, like Mr. Carter, that there is a reasonable risk that if this release, as modified on the record, did not remain in the plan, the Released Second Lienholders would withdraw their support of the plan. This reasonable risk is especially significant, moreover, given all that the Released Second Lienholders have committed to do under the plan.

Nevertheless, I think that the released parties' substantial consideration should be weighed against, in some measure, the claims that are being asked to be released and, where they're being actively pursued, as is the case with the carved-out litigation, ensure that such claims are not frivolous or back-door attempts to collect from the reorganized debtors notwithstanding the discharge. Thus, I believe that it is appropriate to maintain jurisdiction over such litigation, as provided in the modified release, for the same reasons that Judge Gerber has discussed in a number of opinions, including In re BearingPoint, Inc., 453 B.R. 486 (Bankr. S.D.N.Y. 2011), and In re Motors Liquidation Company, 447 B.R. 198 (Bankr. S.D.N.Y. 2011): that, in order to be able to sort out whether a suit is, in large measure, a strike suit or looking to get a

recovery from the reorganized debtor through the artifice of proceeding against a third party or, on the other hand, sets forth a genuine claim that would not be covered by the bankruptcy plan or for which there's not sufficient value being provided by the released parties, the court should, at a minimum, keep jurisdiction over the matter. This also avoids the potential for conflicting orders in different courts and the assertion in other courts of positions notwithstanding the doctrines of collateral estoppel and res judicata, which, based on oral argument, I have serious concerns over here. And I do not believe that the Released Second Lienholders or other courts should be subjected to a potentially multi-court process with respect to the pending Intercreditor Agreement litigation and enforcement of this Court’s confirmation order.

I also should note, because this was raised in the objection, that I firmly believe that I have jurisdiction over this issue for the reasons that I stated at the beginning of this ruling, and that I can issue a final order on it within the confines of Stern v. Marshall, given that this is in the context of the confirmation of the plan, and pertains ultimately to the debtors' rights under the Bankruptcy Code. That would hold true, even post-confirmation or with regard to a post-confirmation effect on the estate. See, for example, In re Quigley Company, 676 F.3d 45, 53 (2d Cir. 2012), cert. denied, 133 C. Ct. 2849 (2013); In re Chateaugay Corp., 213

B.R. 633, 637-38 (S.D.N.Y. 1997), and In re Lombard-Wall, Inc., 44 B.R. 928, 935 (Bankr. S.D.N.Y. 1984).

So, were the plan to be amended as I have said I would find to be appropriate with regard to the cramdown interest rates, I would confirm the plan as it otherwise stands, including the amended release provision.

I believe that covers all of the outstanding confirmation issues. As I said before, to the extent that these issues also overlap with issues that have been raised in the three adversary proceedings covered by the confirmation procedures order, those issues have been decided at this time as well; therefore, I need an order in those proceedings, regardless of what you do with amending the plan.

Dated: White Plains, New York
September 9, 2014

/s/ Robert D. Drain
United States Bankruptcy Judge